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DELIVERED PRICING

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LAW AND CONTEMPORARY PROBLEMS

DUKE STATION — DURHAM, NORTH CAROLINA

LAW AND CONTEMPORARY PROBLEMS

VOLUME 15 SPRING, 1950 NUMBER 2

FOREWORD

Delivered pricing systems, in one form or another, have been firmly entrenched in the economy of the United States for many years. The development of nation-wide markets by sellers, taking advantage of speedier, cheaper, and more efficient forms of transportation and communication, when coupled with the physical distances comprehended in any such marketing area, has inevitably emphasized the possibility of selling on a delivered price basis. When such basic industries as steel and cement have constructed over a long period of time elaborate price structures of this type, it is evident that any attempts either to alter substantially or to abolish this form of pricing are certain to encounter strenuous opposition. In spite of this opposition, these attempts have increased rather than diminished. The fact that delivered pricing systems have, at least to some extent, admittedly been used as one weapon of conspiracies or combinations to fix prices and so restrict or eliminate competition and encourage monopoly—and many would say that their use has almost invariably been in connection with monopolistic price-fixing activities—has meant that these systems have become enmeshed in the toils of the antitrust laws.

The battle over the causes, effects, and merits of various delivered pricing systems has been furiously fought in several areas. Economists themselves have sharply disagreed as to the effects and remedies. The fight before the FTC and the courts has been long and bitter, and still continues. Recently the struggle has shifted to Congress, where the outcome is seriously in doubt. Unfortunately, as Professor Latham so skillfully shows in the case of Congress, the din, fury, and intensity of the debates have too often, as a result of the heavy pressures brought to bear on the participants, resulted in name calling and emotional appeals to free enterprise, and stock denunciations of bureaucratic interference with American business, so that the real issues and arguments have been, sometimes it seems almost deliberately, confused rather than clarified, with the participants themselves sometimes almost inexplicably changing their positions. Of late there have been vehement appeals for clarity and certainty above all else in the law relating to delivered pricing systems; yet the remedies often proposed appear to take the form of legislative action which would seem to create more problems of ambiguity and interpretation for lawyers, administrators, businessmen, and courts than it would solve. One can-

not help wondering, therefore, if the pinch comes from the clear-cut bite of the present laws against delivered pricing systems rather than from their confused imprint. The real issues may be not the alleged confusion of the law, but rather the extent of the relationship between delivered pricing systems and monopolistic and competition-restraining conspiracies and practices, as well as the relationship between the underlying policies of our antitrust laws and the type of economy we desire to have in the United States.

ROBERT KRAMER.

GEOGRAPHIC PRICE STRUCTURES

Charles E. Landon*

I

Introduction

When the businessman quotes a price for his product, he must, in the long run, set an amount which covers his manufacturing and selling costs and which makes allowance for various conditions of sale, one of the more important of which is the incidence of the freight charges. The cost of transportation must somehow be included in the final price of a commodity. The different methods and practices for accomplishing this end—for distributing freight charges among buyers and sellers—have developed certain patterns called *geographic price structures*. These structures vary from industry to industry and within industries or even within firms, but whatever the geographic pricing method, it determines the amount of freight costs each buyer must pay in the purchasing of a product.

The form of the geographic price structure for any commodity reflects the operation of numerous factors, the more important of which are "the intensity and focus of competition including the relative emphasis upon price or nonprice rivalry, the degree of geographic concentration of the industry, the location of sources of supply in relation to markets, the relative importance of transportation costs as an element in the price of the commodity, the channels of distribution utilized, the extent of economic concentration among sellers and among buyers, the interest of sellers in maintaining control over resale prices and conditions, etc."[1] The way in which these factors are reflected in price structures is influenced much by the freedom possessed by individual sellers or groups of sellers in formulating and maintaining price policies.

Pricing policies "affect competitive relations among producers, price levels, product structures, forms of retail and wholesale distribution, existence of branch plants, the degree of vertical or horizontal integration, and many other important aspects of the industrial structure."[2] Pricing policies also exert an influence upon the location of industry.

Generally speaking, the pricing policy of an industry will be determined by two broad sets of conditions: (1) the direct effect of the final price upon consumers

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[1] S. Nelson and W. F. French, Jr., Geographic Price Structures, pt. II, 275 (TNEC Monograph 1, 1940).

[2] G. Ackley, *Price Policies*, in Industrial Location and National Resources, National Resources Planning Board, c. 18, 302 (1943).

of the product and (2) the competitive relationships among the sellers of a commodity.[3] Relative to (1), the geographical pattern of demand affects pricing policies. In respect to competition, there may be price policies to prevent the entry of rival producers into the field, there may be pricing methods to stabilize relations among existing competitors, or a strong firm may go so far as to drive actual competitors from the field.

Another aspect of competition is product differentiation. The greater the differentiation, the more independent the price of a product becomes of its rivals. Under such conditions sales areas are not exclusive, but overlap.

II

TYPES OF GEOGRAPHIC PRICE STRUCTURES

Fundamentally, there are two types of geographic price structures: (1) point-of-origin prices and (2) destination prices. The first type is known variously as f.o.b. point-of-origin, f.o.b. shipping point, and f.o.b. mill prices. "F.o.b." means "free on board," or the delivery free of charge by the shipper to the means of conveyance at the shipping point.[4] Destination prices are commonly known as "delivered" prices. Reference is usually to delivery at a railroad destination, but delivery to a plant warehouse or retail outlet of the buyer may also be included. Generically, a delivered price, *i.e.*, the price quoted to the buyers, is the sum of two prices: (1) the seller's price plus (2) the transportation charge to the buyer's destination.[5] Delivered prices exist in several variations and combinations which often seem to blend into each other. It is therefore not always easy to distinguish particular applications except by careful examination and analysis. F.o.b. point-of-origin price structures are relatively simple, but delivered price structures may and do become complex.

Various influences underlie delivered prices. "Historical development and long-established custom have played their part in some industries. Trade-association activity has had its influence in others. The sale of products under nationally advertised brands may in some instances be a determinative factor. Inadequacy of price competition will probably account for the delivered price in many industries.

"Probably the most important single determinative factor in adopting the use of the delivered price uniform for all destinations is the ratio of delivery cost to total production and delivery cost."[6]

[3] For more details on these points than can be given here, see Ackley, *Price Policies*, *supra* note 2.

[4] The term "c.i.f." (cost, insurance, freight) is often used in connection with water shipments. Under this arrangement the quoted price includes insurance and freight to a specified port and delivery in good condition to other means of conveyance at the port, with the buyer bearing the expense and risk of further transportation. Under the term "c.i.f.e." the quotation includes a provision for converting foreign exchange. With "c. & f." the buyer must arrange for insurance on a water shipment. Under still another arrangement, "f.a.s.," meaning "free alongside," the buyer accepts delivery at the wharf and must arrange for loading for overland shipment. NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1.

[5] Fetter, *Exit Basing Point Pricing*, 38 AM. ECON. REV. 815, 817 (1948).

[6] FTC, PRICE BASES INQUIRY: THE BASING-POINT FORMULA AND CEMENT PRICES 13 (1932)

Hereafter, in this discussion, the two preceding types of price structures will be designated as "f.o.b. mill" prices and "delivered" prices.

The relative importance of f.o.b. mill prices and delivered prices in manufacturing in the United States is indicated in the following table, in which are shown the results of a survey made by questionnaire by the Federal Trade Commission.[7] Percentages, it should be noticed, apply to the number of firms included in the survey and not to the volume of business. The volume of sales for each method of pricing might be either much higher or much lower relatively than is indicated by the number of firms using a particular method. Although the data are for 1928, in view of subsequent developments, they probably give a fairly representative picture of later conditions. Later compilations of this nature are not available.

In this table approximately 44 per cent of the reporting firms employed f.o.b. mill pricing, 18 per cent delivered pricing, and 38 per cent both f.o.b. mill and de-

TABLE

Number of firms reporting to the commission, by industry groups, together with number selling exclusively on point-of-origin prices and on delivered prices and with number selling on both classes of prices.*

Industry group	Total number firms in each industry group reporting	Number of firms with all sales on f.o.b. point-of-origin prices		Number of firms with all sales on delivered prices		Number of firms with sales on both f.o.b. point of origin and delivered prices	
		Number	Per cent total reporting	Number	Per cent total reporting	Number	Per cent total reporting
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Food and kindred products	529	122	23.06	189	35.73	218	41.21
Textiles and their products	347	236	68.01	28	8.07	83	23.92
Lumber and allied products	493	154	31.24	114	23.12	225	45.64
Paper and paper products	138	72	52.17	14	10.15	52	37.68
Printing and publishing and allied industries	166	103	62.05	20	12.05	43	25.90
Chemicals and allied products	266	77	28.95	75	28.19	114	42.86
Products of petroleum and coal	41	22	53.66	2	4.88	17	41.46
Rubber products	50	1	2.00	23	46.00	26	52.00
Leather and its finished products	135	88	65.19	6	4.44	41	30.37
Stone, clay, and glass products	261	80	30.65	39	14.94	142	54.41
Iron and steel and products, except machinery	307	120	39.09	47	15.31	140	45.60
Nonferrous metals and their products	206	88	42.72	28	13.59	90	43.69
Machinery, except transportation equipment	275	162	58.91	18	6.54	95	34.55
Transportation equipment	100	81	81.00	4	4.00	15	15.00
Miscellaneous industries	329	199	60.49	43	13.07	87	26.44
Total of firms in all industry groups	3,643†	1,605	44.06	650	17.84	1,388	38.10

*The reports to the commission on which the table is based were made early in 1928. The column numbers have bee n supplied by the author.

†The actual number of different firms represented by this total is 3,561 because of the instances where the same firm ap pears in more than one industry group.

[7] *Id.* at 10.

livered pricing. The relative importance of the two price systems in the case of firms selling wholly or in part on an f.o.b. mill basis was determined by the Federal Trade Commission by combining the data for columns (2) and (6) of the preceding table. Such an analysis showed that approximately 15 per cent of the 2,993 reporting firms with f.o.b. mill prices made all or a part of these prices with partial freight allowances.[8]

Geographic pricing policies have been variously classified, depending upon the purpose or the concept of the particular writer.[9] Because the different types of price structures represent an evolutionary process, and hence blend into each other, it is difficult to draw distinct lines between them. Any classification seems to involve overlapping. For the purposes of discussion here, the following classification is used:[10]

I. F.o.b. mill price systems
II. Delivered price systems
  A. Freight equalization systems
    1. Unsystematic
    2. Systematic
  B. Basing point systems
    1. Single
    2. Multiple
  C. Zone price systems
    1. Single zone
    2. Multiple zone
  D. Unsystematic price variation

The relative importance of the different classes of delivered prices is shown in the aforementioned survey made by the Federal Trade Commission. The total number of firms with such prices was obtained by combining columns (4) and (6) of the preceding table and it includes firms making all or a part of their sales on a delivered price basis. The results were as follows:[11]

Firms with delivered prices uniform for all destinations	36.21 per cent
Firms with delivered prices uniform for zones	26.74 per cent
Firms with delivered prices made on basing point plan	8.25 per cent
Firms with delivered prices unclassified	28.80 per cent
	100.00 per cent

[8] *Id.* at 11, table 2.

[9] Classifications of geographic price structures are available in the following sources: A. R. BURNS, THE DECLINE OF COMPETITION 280-290 (1936); E. M. HOOVER, THE LOCATION OF ECONOMIC ACTIVITY, c. 4 (1948); J. F. FREDERICK, INDUSTRIAL MARKETING, c. 8 (1934); F. MACHLUP, THE BASING-POINT SYSTEM 3-17 (1949); Ackley, *Price Policies*, *supra* note 2, at 302-303 (1943); FTC, PRICE BASES INQUIRY: THE BASING-POINT FORMULA AND CEMENT PRICES, *supra* note 6, at 5-9; NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1, at 269-285; G. SEIDLER, THE CONTROL OF GEOGRAPHIC PRICE RELATIONS UNDER CODES OF FAIR COMPETITION (NRA, DIVISION OF REVIEW, WORK MATERIALS No. 86) 6-10, 28-50 (1936); C. Kaysen, *Basing Point Pricing and Public Policy*, 63 Q. J. ECON. 289, 292-293 (1949).

[10] This classification is adopted from those in FTC, PRICE BASES INQUIRY, *supra* note 6, at 5-9, and NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1, at 277-285.

[11] FTC, PRICE BASES INQUIRY, *supra* note 6, at 12, table 3.

In this survey of the Federal Trade Commission the delivered price systems are not divided as they are in the preceding outline. The columns headed "Number of firms with delivered prices uniform for all destinations" and "Number of firms with prices uniform for zones" apparently include categories A and C of the outline.

The Federal Trade Commission study shows (1) that in many industry groups the percentage of firms using both f.o.b. mill and delivered prices is high and (2) that a large percentage of the reporting firms in every industry group use both methods. The former situation is explained by the differences between industries in respect to the products made, size and location of plants, degree of integration, and other factors. The second condition can be accounted for by the fact that any one firm may sell several different products under a variety of conditions, and that some firms have plants at different locations selling the same product under widely differing competitive, producing, and marketing conditions.

A. F.O.B. Mill Pricing

Under f.o.b. mill pricing, each seller has an announced mill or base price which is the same for all buyers at a given time. The buyer selects the mode and route of transportation and pays the freight charge to the destination. He also normally assumes title at the shipping point and therefore assumes the responsibility for presenting to the transportation agency any claims for loss or damage. The price of the commodity to the buyer rises as his distance freight-wise from the shipping point increases. All sales therefore return the same mill-net price to the seller. Such a pricing system limits the geographic radius of competition, assuming equal base prices for all producers, to the weight of the freight charges. There is a natural division of markets between rivals based on transportation costs. Whether sellers have the same or different mill prices, the market of any seller extends to the point where the sum of his base price plus freight charges is equalized with that of a competitor. The size of a seller's market will be changed by changes in his base price or in the freight rates he pays, or both.

The simplest sort of case is that of two manufacturing points having the same base price for a product and with equal mileage scales outward from them. Their market areas will be divided by a straight line half way between them and perpendicular to the line connecting them (see Figure 1).

If the freight rates from A are on a lower level than those from B or if the mill price at A is lower, or if a combination of base price and freight charges results in a lower sum than does such a combination from B, the market of A will be enlarged. The point at which the combination of base price and transportation cost is equalized will have shifted toward B, and the line separating the two markets will no longer be a straight line, but will be a hyperbola which bends around the market with the higher combination of base price plus transportation.[12] This situation is illustrated in a generalized manner by the dotted line in Figure 1.[13]

[12] This subject has been developed thoroughly by F. A. Fetter in *The Economic Law of Market Areas*, 38 Q. J. ECON. 520-529 (1924), and in THE MASQUERADE OF MONOPOLY (1931).

[13] Obviously, this illustration applies to a selling, or dispersing, market. For a buying, or con-

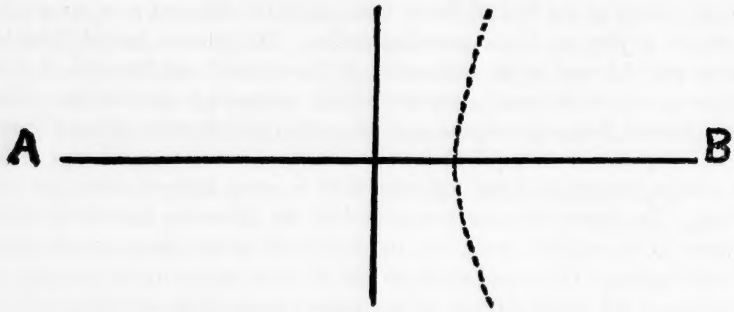

FIG. 1

Under f.o.b. mill pricing there is no relationship between the mill prices of the various sellers. Owing to differences in the costs of production at the various locations, the selling prices of mills are not likely to be uniform except at some points and in marginal zones between mills. In the long run, f.o.b. mill pricing will tend to bring prices down to the low point of actual cost, and further, will encourage the search for improved methods of production in order to obtain cost advantages over competitors. In a deficit area for a product, a producer can raise his price temporarily to that of the nearest competitor plus freight charges from the latter's location. But high profits enjoyed by the former producer would encourage him to expand his operations, and the added supply of product would cause the price to tend downward toward his cost of production.

It should be noticed that blanket freight rates will modify the operation of an f.o.b. pricing system.[14] Blanket rates average the freight charges of groups of shippers, thus forcing the carriers to absorb freight on some shipments and to receive excess charges on others.

F.o.b. mill pricing may be employed when there is a lack of competitive pressure, with the sellers all being located in a restricted geographic area, so that all of them have practically the same shipping costs to the same markets. In such situations it is the usual policy of the railroads to give all sellers the same freight rates by the establishment of a group rate, which is similar to a blanket rate except that it covers a smaller area. F.o.b. mill prices are difficult to maintain unless all producers are located in a single area. The reasons for this condition are discussed later in the section on freight equalization.

F.o.b. mill prices are easy to apply also, when freight charges are a negligible proportion of the final price, when non-price factors such as style are emphasized, and when competing products are different in quality and design, even though the

centrating, market, such as the large primary markets for farm staples, the situation would be the reverse, *i.e.*, the market which offered the higher price would have the larger marketing territory, with the boundary curving around the point offering the lower price.

[14] Blanket freight rates are those which are uniform for a commodity over large areas. For example, the rate on oranges from California was at one time uniform over most of the country east of Denver.

freight charge is a substantial portion of price. The system is used in the pricing of light consumer goods, furniture, turpentine, phosphate rock, automobiles, agricultural implements, Lake Superior iron ore, and nonferrous scrap metal. The price structure of the last product is controlled largely by buyers.[15]

Some prices nominally classified as f.o.b. mill prices may fail to meet the foregoing requirements and must therefore be classified as delivered prices. This matter is treated in the following section. On the other hand, there are those who classify f.o.b. mill prices as delivered prices.[16] Such prices are delivered prices in the sense that there must always be a final price at the destination, which, in the case of f.o.b. mill prices, is the sum of the mill price plus freight charges. This price is the delivered price so far as the buyer is concerned—it is the total price which he pays—but it is not a delivered price in the sense in which that term has already been defined.

B. Delivered Prices

Under a system of delivered prices, the price paid to the seller includes both the mill price and the transportation charge, but most buyers do not pay the actual freight charge on their shipment; they pay either more or less. If the buyer pays less, the seller must bear the difference, a practice which is called ***freight absorption***; if the buyer pays more, the seller receives more than he actually pays for freight, the difference being called ***phantom freight.*** Unlike f.o.b. mill prices, delivered prices do not reflect relative transportation costs. Under the former system no buyer helps pay for the freight charges incurred on the part of some other buyer. Delivered pricing differs from f.o.b. mill pricing in the opportunity offered by the former for discriminating in price between different sales areas. Geographic price discrimination occurs when, after the deduction of transportation charges, the mill-net price varies with the geographic location of buyers. The difference between the mill-net price on any sale and the highest mill-net price received on any sale of the same product measures the amount of freight absorption on a sale, ignoring special discounts or unsystematic price concessions.[17]

Delivered prices result in either (1) the payment of an average freight rate by all buyers of a product or by zones of buyers; (2) the payment of freight charges based on the distance from some production point or distribution point, no matter what the actual distance from the producer to the buyer may be; or (3) the payment of an equalized freight charge from the mill nearest the buyer regardless of the location from which the purchase is made.[18] All of these practices result either in phantom freight or freight absorption. Freight absorption exists in all geographic price structures except f.o.b. mill pricing and except for producers located at the

[15] Nelson and French, Geographic Price Structures, *supra* note 1, at 343.
[16] Ackley, *Price Policies*, *supra* note 2.
[17] *Id.* at 303.
[18] Seidler, The Control of Geographic Price Relations Under Codes of Fair Competition, *supra* note 9, at 28-29.

basing point under a single basing-point pricing system.[19] Freight absorption discriminates against the nearer buyers, and its use makes competition possible in remote markets. Discrimination against remote buyers is rare, but it is practiced occasionally by industries in which the producers are highly concentrated geographically.[20] The most frequent form of freight absorption is that involving a uniform delivered price, either nationally or by zones.[21]

Some f.o.b. mill price arrangements are actually delivered prices. This is true when the seller, instead of prepaying the freight charges, may sell on a basis of "transportation charges allowed" to a specific destination, under which the buyer pays the transportation costs but is allowed an equal credit by the seller. This method is the opposite of an "f.o.b. destination price," under which the seller prepays the freight charge but adds the amount to the invoice of each buyer, making the method actually an f.o.b. mill price system, except that in this type of case the title may change hands at the destination, in which event the seller would be responsible for presenting to the carrier any claims for loss or damage. This practice, however, is not common.

Although practically, when the buyer pays the freight but deducts the amount from the invoice or the seller prepays the freight, the resulting prices are f.o.b. mill prices, such arrangements may affect cash and other discounts which may be calculated on the gross amounts as a base.

If a seller gives freight allowances or in any way pays part of the freight or collects more freight than he actually pays, the pricing system is not an f.o.b. mill one.

When allowing freight, some firms do not use the actual charge to each buyer's destination, but rather, use approximate allowances which average the freight charges to various points in a territory. Each buyer uses the allowance to the point nearest his station. Under a system of freight allowances, the buyer may select the mode of transportation and he also assumes the responsibility for presenting loss and damage claims to the carrier.

When f.o.b. destination prices are employed it is easy for a buyer to compare the final prices of the different sellers, but unless the buyer knows the freight charges from different locations, it is difficult for him to compare mill-net prices, particularly if the delivered price varies directly with the freight charge in all cases.

An important reason for delivered pricing systems is the ease with which producers may police their prices. Violations of a price formula are conspicuous. The number of different prices is also reduced, which is an aid to the buyer in the comparison of prices of different sellers and at different locations. One of the first arguments put forth to justify basing point pricing was that buyers wished to know how much a product cost delivered.[22] Also, the exchange of market information among producers is made easier because of the uniform basis for reports.

[19] Ackley, *Price Policies*, *supra* note 2, at 303.

[20] HOOVER, *op. cit. supra* note 9, at 55.

[21] *Id.* at 56.

[22] Fetter, *Exit Basing Point Pricing*, *supra* note 5, at 815, 817.

So long as producers act spontaneously and are free to change prices to meet the individual producer's own conditions or markets, most delivered price systems tend to bring actual pricing close to the level that would prevail under a condition of individual competition. But when they are set up by some producers and enforced on others, individual action is prohibited. Any advantage which the individual producer possesses or has developed cannot be freely translated into a price to expand his own market.[23]

C. Freight Equalization

Freight equalization occurs when there is more than one geographic source of supply for a commodity and producers try to expand into or penetrate each other's markets and must therefore compete in neighboring market areas with sellers who are located nearer the buyer freightwise. There are two forms of freight equalization, namely, unsystematic and systematic. The first type occurs when a seller reduces the price on a particular transaction to meet the offer of a better located competitor. The second type, which is also known as the "mill-base system," exists when a pattern of prices is observed by most or all of the competing sellers on intermarket sales. The principle assumes generally the uniformity of mill prices, which makes it possible for a producer to ascribe a higher mill price to quality or service.[24] With a freight equalization system, the mill-net price is reduced on distant sales but sales to nearby buyers, *i.e.*, those for which a particular seller has a freight advantage, are still made on an f.o.b. mill basis. The location of each mill governs the price in surrounding territory, and the erection of a new plant in a new territory will be reflected automatically in the delivered price in that territory.[25]

These conditions are illustrated in Figure 2. In this diagram it is assumed that freight rates are on a distance basis and that mills A, B, and C each has a price advantage on sales within the lines that enclose each one. The dividing lines are lines along which the prices between different mills (the sum of mill price and freight rates) are equalized. If C wishes to sell at e or f, it would have to meet the price of A and B, respectively, at those places. The same sort of situation would prevail if either A or B, or both, tried to sell in the other two market areas.

Now, suppose that a new mill is built at f. This mill, assuming a base price which is competitive with A, B, and C, will have an area over which it will have a freight advantage, and prices in that area will no longer consist of the mill B price plus transportation from B, but of the mill f price plus transportation from f. If A, B, and C sell in the territory of f, they will have to meet that price. Any mill erected at a new location will effect such a change in delivered prices in its natural market area.

By this time the reader may have become aware of a possible reason for the development of systematic patterns of prices which all sellers may observe in mak-

[23] E. G. NOURSE AND H. B. DRURY, INDUSTRIAL PRICE POLICIES AND ECONOMIC PROGRESS 137-138 (1938).

[24] FREDERICK, *op. cit. supra* note 9, at 293.

[25] NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1, at 279.

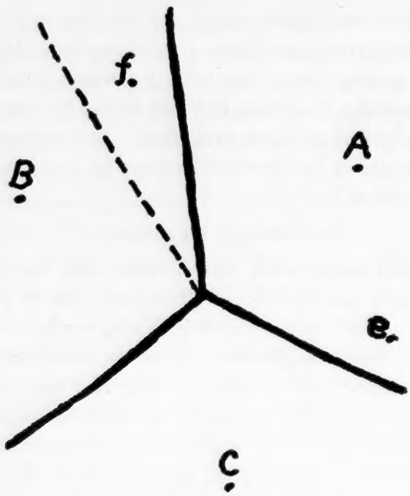

FIG. 2

ing sales outside their own natural market area. Apparently, price competition would be limited by such a procedure. Also, as is explained in the next section, patterns of systematic freight equalization could provide the basis on which a system of multiple basing point pricing might develop.

Market penetration may develop naturally when a producer with an f.o.b. mill system outgrows his local market or has a temporary surplus of output which cannot be absorbed by the territory he has customarily served and must therefore be sold in the natural market of some other producer. He sells there by meeting that producer's price while maintaining another price in his local market. If his base or mill price is the same as that of his competitor, he sells in the competitor's market by adding the freight rate charged by his rival to his own base price, thus equalizing the two prices. In this manner, every producer may be selling in the markets of several others. In any particular market, all the producers charge, not the actual freight incurred by each one, but the lowest incurred by any of them. In the type of situation just described, each producer acts individually and spontaneously, and, consequently, the system is one of unsystematic freight equalization.

Systematic freight equalization takes place when the preceding type of situation results in price patterns which are observed by all sellers and which are too complicated to have arisen spontaneously. Such systems often spring from an effort of the firms in a field to limit price competition rather than from natural adjustments to the market.

Any method of delivered pricing based on freight equalization or on an average freight rate makes possible the extension of markets far beyond the limits set by f.o.b. shipping point pricing and enables a mill to ship a great distance from its

normal market, particularly if mill prices can be maintained considerably above the competitive level. Delivered prices grow out of conditions that would lead to the overlapping of market areas, even in the absence of any formal arrangement.

Industries in which unsystematic freight equalization occurs in pricing include those producing industrial machinery, douglas fir, gasoline, and bituminous coal. Industries in which systematic freight equalization exists in pricing products include those producing salt, binder twine, many building materials, and numerous heavy chemicals. Among the building materials are lime, floor tile, sewer pipe, prepared roofing, glass, gypsum plaster, and boilers. The heavy chemicals include sulfuric acid, soda ash, acetic acid, nitrocellulose, hydrochloric acid, calcium carbide, and others.[26]

D. Basing Point Pricing

A basing point is a geographic point from which prices to buyers are computed. The dominant feature of a basing point pricing system is the creation of a fixed, well-defined price structure with the delivered prices of all sellers being identical for a single customer, regardless of the location of the seller. For any than a mill located at a basing point the price charged the customer is the sum of another mill's base price plus what the freight charge would be if the commodity were shipped from that mill. Buyers who purchase from the basing point in their territory pay the actual freight charge; other buyers pay either more or less. At points that are nearer to it freightwise than they are to the mill which governs the delivered price, a non-basing point mill collects phantom freight, *i.e.*, it collects more in freight charges on a shipment than it actually pays the carrier. When a base mill sells in a territory where the price is governed by another basing point, it absorbs freight, *i.e.*, it pays more in freight charges to the carrier than it collects in freight from the buyer. Any mill which is farther freightwise from a buyer than is the basing point mill must absorb freight on such sales. The effects of such a pricing system are to neutralize the influence of location freightwise on the prices of competing sellers and to differentiate the net price or yield at the mill according to the location of the buyer. In other words, the sellers discriminate among buyers as to price.

Basing point pricing discriminates between buyers for two reasons. (1) The mill-net yield of non-basing point mills varies with the differences between the cost of transportation from the basing point and that from the actual point of production. (2) Even though every point is a basing point, sellers absorb freight on sales to points that are more cheaply reached by competitors.[27]

The preceding features are illustrated in Figure 3. In this diagram, B represents the basing point in a single basing point system; N, a non-basing point mill; and C and M, two different markets. A base price of $40 a unit of product is assumed, with transportation charges as shown by the numbers between the dif-

[26] *Id.* at 344-345.
[27] See BURNS, *op. cit. supra* note 9, at 290.

ferent points. The price of a unit of product at C is $40 + $3.00, or $43. The price in C of a product from N is likewise $43, but N charges $3.00 in freight but pays actually only $1.00. The difference of $2.00 is phantom freight. Further, suppose that at N the cost of production were only $35 a unit, whereas N is compelled to charge as though it were $40. The possible effect of the profit as a stimulus to

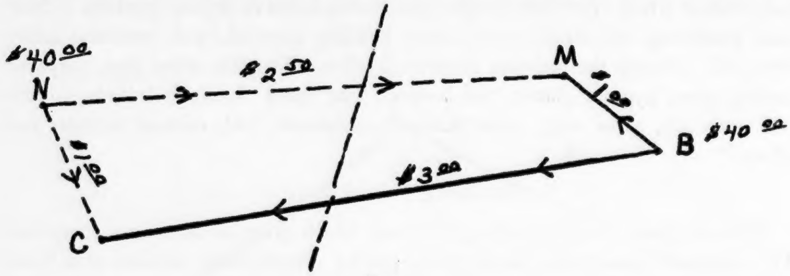

FIG. 3

new capacity at N is evident. At M, the price would be $40 + $1.00, or $41. If N sells at M it must sell at $40 plus $1.00 for freight, or $41, but must actually pay $2.50 to the carrier. On sales at M then, N would be compelled to absorb $1.50 per unit of product in freight charges.

The same diagram may be used to illustrate a multiple basing point system. The only difference between this and the preceding situation would be that N now becomes the controlling basing point at C, where the delivered price would become $40 + $1.00, or $41, instead of $43 as previously. On sales at C, B would charge only $1.00 in freight but would actually pay $3.00, being compelled therefore to absorb $2.00 a unit of product. In this instance B realizes a mill-net price of $40 on sales at M, and of $38 on sales at C. N realizes a mill-net yield of $40 on sales at C, and of $38.50 on sales at M. Evidently, there is discrimination in prices as between differently located buyers of a given seller.

Usually under a basing point system all prices are not alike and all locations are not basing points. In a true basing point system there will always be some plants which are not located at any basing point.[28] The system may be employed for the scattered plants of one firm or for several independent producers located at different places.

Usually, two types of basing point systems are distinguished, namely, single and multiple. The former type commonly grows out of a situation in which one producer or one producing center is or has been dominant in the industry. According to one authority, basing point pricing is a practice which will perpetuate the position of advantage a firm has been enjoying, it being essential for the older firms of an industry and their different dependent economic interests that transfer of production to new regions be retarded as much as possible.[29] Such a price policy

[28] *Ibid.*; NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1, at 273.
[29] NOURSE AND DRURY, *op. cit. supra* note 23, at 136-137.

is also often the outgrowth of price leadership by a dominant firm or of a situation when all the firms are in one area but are not grouped closely enough so that all can have the same freight rate to any market.[30]

Under a multiple basing point system the price to any given buyer is the lowest combination of mill price plus freight, regardless of the location of the mill from which the customer buys. Some multiple basing point systems, as for steel and cement, have evolved from a single basing point system. Other such systems have developed independently out of f.o.b. mill price systems by sellers trying to expand their markets at the expense of rival producers but trying also to avoid price warfare. The desire to match the prices of those nearest the markets and to avoid retaliatory dumping has led, often by agreement, to systematic price structures which establish price relationships by formula. The basing point system is the most important of such methods. Still other multiple basing point systems may have been adopted by agreement among producers who had been practicing systematic price equalization. This procedure would simplify the price structure of a particular industry and would provide publicity of prices throughout the industry so that a producer would not unknowingly cut under the prices of other producers.[31] Sometimes there may be a conspiracy to fix prices, the basing point system being used as a means to this end. Many geographic price structures have not sprung from natural adjustments to the market but rather from the conscious effort on the part of firms in an industry either to limit or to prevent price discrimination, for which they may be indispensable tools.[32] The choice of common basing points in an industry apparently presupposes some form of agreement or understanding.[33] Under basing point pricing a definite price is fixed for each locality by means of a formula method of selling.

Multiple basing point pricing appears to be similar to systematic freight equalization, and some authorities classify freight equalization as a multiple basing point system with all plants being basing points and with all mill prices being alike.[34] All competitors charge the lowest rate incurred by any of them rather than the actual cost of transportation. However, under freight equalization, each mill governs the price structure in its natural market or surrounding territory, and, as was stated previously, the erection of a new mill in a new territory will be automatically reflected in the prices for the product in that territory. This is its chief difference from the multiple basing point system.

An increase in the freight rate from a basing point to a market which remains in its territory after the increase becomes effective will result in an increase in the price of the commodity in that territory. However, it will not necessarily cause a reduction in the share of the sales made there by producers located at the basing

[30] Ackley, *Price Policies*, *supra* note 2, at 307.
[31] *Ibid.*
[32] NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1, at 278.
[33] G. A. Stephens, *Basing Point Pricing*, in I ENCYC. SOC. SCI. 473, 474 (1937).
[34] FREDERICK, *op. cit. supra* note 9, at 293.

point nor an increase in the sales of plants at locations which did not have an increase in their freight rates.

Basing point markets are characterized by (1) a high degree of standardization of product, for example, steel and cement; (2) a low value per unit of weight, causing the freight rate to be a substantial portion of the delivered price of the commodity; (3) heavy overhead costs, making the efficient scale of manufacturing operations for a firm large; (4) production frequently below full capacity; (5) specialized and long-lived production equipment; (6) market demand that is usually inelastic at and below prices which correspond to output considerably less than full capacity; (7) the prevalence of oligopoly, because of the small number of producers; and (8) production and markets that are both widely scattered.[35]

Basing point pricing requires certain essential features: (1) basing points and base prices that are publicly known in the trade, (2) uniquely defined freight costs from every basing point, and (3) always considerable market interpenetration, *i.e.*, a mill selling at a point which, on the basis of mill price plus the transportation charge, could be supplied by other mills at a lower price.[36]

There is usually a common compilation of freight rates in the form of a freight book used by all firms in an industry. Usually, but not always, the rates are the actual rates paid to the transportation agency. The rates charged are also usually the all-rail rates regardless of the mode of transportation employed.

Market interpenetration results in geographic price discrimination. With a multiple basing point system there usually is freight absorption and always selling costs in excess of what would be spent without market interpenetration. Basing point pricing permits selling at distant points if the general level of such prices is high in relation to the costs of manufacture. It is contended that the system encourages keen competition in business, but little competition in price. Price stability is attained without reducing competition. To avoid loss, the basing point price level must, in the long run, be raised by at least the amount of freight absorption reduced to a price unit basis.[37] In other words, the general level of prices for the commodity is forced above the level which would prevail in a freely competitive system by at least the amount of the extra cost resulting from market interpenetration or crosshauling.[38]

There may also be a natural division of markets under a basing point system. A seller may concentrate his sales in an area from which he collects phantom freight and refrain from soliciting business in markets in which he would have to absorb freight.[39]

Products which have been sold under a single basing point system are maple flooring, zinc, copper (except lake copper), industrial benzol (Omaha and West),

[35] For the first seven points, see Kaysen, *Basing Point Pricing and Public Policy*, 63 Q. J. ECON. 289, 290-291 (1949). Point (8) is from FTC, PRICE BASES INQUIRY, *supra* note 6, at 13, 14.

[36] Kaysen, *supra* note 35, at 291-292.

[37] FREDERICK, *op. cit. supra* note 9, at 292.

[38] See note 33 *supra*.

[39] C. F. PHILLIPS, MARKETING BY MANUFACTURERS 281 (1946).

and gasoline (group 3 district, but with considerable variation).[40] In the days of Pittsburgh-plus, Pittsburgh was the single basing point for the steel industry. Birmingham has been a single basing point for cast-iron soil pipe.

Commodities which have been sold under a multiple basing point system include steel, cement, wood pulp, sugar, southern pine, oak flooring, lead, and others.[41]

E. Zone Pricing

A zone pricing system may have only a single zone covering the entire country or there may be multiple zones. With a single zone, prices are quoted according to the "postage-stamp method," *i.e.*, there is a single uniform delivered price for all buyers. The aggregate prices charged are high enough to cover total freight charges, but the near buyers pay more than the actual freight rate to their destination and the distant buyers, less. By accident, some buyers may pay the actual freight charge to their location, but the prices are not arranged to accomplish such a purpose.

The seller usually quotes a single price and prepays all transportation charges. In some cases, however, the buyers may pay only a portion of the freight charges, all buyers being assessed uniformly, with the seller absorbing the remaining portion.[42] Zone prices are then apparently a form of single basing point prices, equal to the sum of a mill price plus some form of average freight rate to the different points in the zone. Such a practice is feasible and is economical and convenient to use when transportation charges are only a small proportion of the final price of an article. It is desirable when a producer wishes to develop a national market through the national advertising of a brand name; the price may be quoted in the advertisement. The system is also an aid in resale price maintenance by a manufacturer.

Under a multiple-zone system, the zones may be large or small, and they may exist in a geographic price structure not wholly based on a zone system. If the freight charge is a negligible part of the final price, zones tend to be large; when freight is important, multiple zones may be used in order that the equalization of freight over a given zone will not create too wide a margin between the average freight rate included in the price and the actual freight charge for each customer. A feature of zone pricing, and a problem in establishing zone boundaries, is the necessary existence of sharp breaks or differences in prices on either side of a zone boundary. A simple type of multiple-zone structure exists for products which have a uniform price east of the Rockies but a higher price in the West and often in Canada.

Under a multiple-zone system of pricing and when products are differentiated, there are infinite variety and combinations of price structures to meet particular situations. When production is not standardized competing sellers need

[40] Group 3, composed largely of Oklahoma, Texas, and Missouri, governs prices through most of the midwest. See NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1, at 341.

[41] *Id.* at 345.

[42] BURNS, *op. cit. supra* note 9, at 285.

not use the same zone boundaries nor quote the same prices in each zone. Neither need prices vary between zones by the same amounts. A zone system of pricing can approximate almost any other system of delivered pricing.[43]

Uniform delivered prices have been employed nationally in pricing many light consumer goods, hardware, business machines, electrical machinery, rayon yarn, manila rope, plumbing fixtures, batteries, coal tar dyes, aluminum, many kinds of electric wire, mahogany, and other products. Multiple-zone pricing has been employed for office furniture, mixed fertilizers, automobile tires, soap, paper and paper products, carbon black, power cable, methyl alcohol, bathtubs, soda ash, cyanamide, linseed oil, nationally advertised prepared paints, mahogany, doors, windows and window frames, the heavier articles of electrical household equipment, some food products, and many other commodities.[44]

F. Unsystematic Price Variation

There are types of geographic price variations which cannot be fitted into any of the preceding price patterns, or into any price pattern, for that matter. In some cases prices may be largely out of the control of sellers;[45] in others, special competitive conditions may require deviation. For such products as brick, sand and gravel, and bread, the markets are so predominantly local that price patterns do not exist, and for other products, including most agricultural commodities and meats, the delivered prices are determined so largely by local market conditions that systematic patterns of price variation are lacking.[46]

[43] Ackley, *Price Policies*, *supra* note 2, at 308.

[44] NELSON AND FRENCH, GEOGRAPHIC PRICE STRUCTURES, *supra* note 1, at 344.

[45] This may be true only temporarily, or there are some instances in which buyers instead of sellers dominate and determine price policy. Buyers may control prices in order not to bid up the prices of raw materials they need. In such cases buyers quote prices which are equalized at the point of shipment. Examples of this policy are nonferrous scrap metal, cottonseed, until recently, at least, and possibly crude petroleum. *Id.* at 284-285.

[46] *Id.* at 345.

THE DEVELOPMENT AND INCIDENCE OF DELIVERED PRICING IN AMERICAN INDUSTRY

VERNON A. MUND*

I

MARKETING PRACTICES PRIOR TO THE RISE OF TRUSTS AND MERGERS

A. The F.O.B. Practice

In the American economy open markets for the basic commodities developed both as voluntary centralizations of private dealers and as formally organized commodity exchanges. By 1860 the principal central markets for iron, steel, and the non-ferrous metals were located in New York, Philadelphia, Pittsburgh, Cincinnati, Cleveland, Chicago, and St. Louis. The task of distributing the metals was largely performed by dealers and jobbers (independent wholesale merchants) who maintained warehouse facilities in the central markets and also on land adjacent to the producing mills. These trade interests purchased commodities from nearby mills or from sources abroad for resale to consuming industries. The products purchased were either shipped directly from the producing mills to the fabricators or placed in storage to await the development of consumer buying.

Merchants and speculators in the central markets performed the useful service of accumulating inventories, at a time when consumer demands were declining, for sale again when business conditions improved. This activity, known as the "balance wheel" function, helped to provide a broad and continuous market for first hand producers and also helped to prevent sharp price declines when the consuming industries were not buying. Thereupon, when the demands of consuming industries revived, the accumulated stocks of merchants and speculators served as a counterbalance to check extreme price advances.

The usual practice followed by various trade interests in the sale of the basic commodities was to quote prices f.o.b. their warehouses in the central markets or f.o.b. the mill if direct delivery was made.[1] If delivered prices were quoted, they were determined by taking the seller's f.o.b. mill or warehouse price and adding the actual freight from the shipping mill to the various destination points. In the

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[1] See, for example, the trade papers of the period, as well as 2 V. S. CLARK, HISTORY OF MANUFACTURE IN THE UNITED STATES 288 (1929). F.o.b. mill pricing means free on board, that is, loaded on cars or trucks at the seller's mill or warehouse with all charges paid up to that point but not including insurance or freight beyond. An f.o.b. price is the price at the freight yard of the origin of shipment. C.i.f. pricing differs from f.o.b. mill pricing in that a c.i.f. price is a composite price which covers payment for three separate items: (1) the f.o.b. mill price or cost, (2) the actual insurance cost, and (3) the actual freight cost to a particular destination. A c.i.f. price always means a landed price at the destination point.

Pittsburgh-Plus case, Henry P. Bope, an executive in the American Steel Corporation, testified that in the steel industry the general practice as late as 1880 was to quote prices f.o.b. the mills. "Each mill," he added, "was a law unto itself."[2]

The f.o.b. mill prices *of a given* seller were also usually uniform to all buyers at the mill or warehouse at a given time. Trade journals and the newspapers provided a considerable amount of price publicity, and the very number of independent dealers, with supplies on hand in the central markets or in storage at or near the producing mills, usually made it impossible for a seller to make some buyers pay more than the "going" price to others. It is true that a locally separate mill sometimes charged nearby buyers more than it received on shipments to buyers in a central market.[3] All of the available evidence, however, indicates that this exercise of local monopoly power was an exceptional practice and not the rule. The general pattern was one of f.o.b. mill pricing in which prices in the local markets and at points of production were *less* than in the central markets and at destination points by the actual cost of freight and handling charges.

B. The Growth of Discriminatory Pricing

The rapid extension of rail lines around 1860, and the rise of towns and consuming points along the main transportation routes made it possible to build larger mills and smelters and to expand greatly the areas of practical shipment. Geographically separate mills, moreover, gradually learned by experience that profits could be enhanced by making direct sales to local buyers at high prices while cutting prices on sales in other areas to match or undercut the quotations of distant rivals. Under such conditions, f.o.b. mill pricing in certain basic industries began to give way to various forms of discriminatory pricing. In order to avoid the evils of local price cutting and also to enhance their profits, a number of regional groups turned to the formation of "pools," "associations," and "loose-knit combinations" through which prices were fixed by agreement.

Monopoly agreements had frequently been made in earlier years by local groups of producers. Such agreements, it appears, were based upon the charging of identical f.o.b. mill prices. When geographically separate mills, however, sought to act as one on price, there at once developed the problem of how all of them could quote identical prices at the important consuming points because geographic location gave certain mills a freight advantage over others. If each locally separate mill had adopted an identical f.o.b. mill price, those nearest to the consuming centers would have secured a major share of the business. The iron bar industry, consisting of a number of geographically separate producers, wrestled with this problem as early as 1875. According to the *American Manufacturer* for May 11, 1875, "The meeting of the Western Iron Association last week was a most important one and was largely

[2] Federal Trade Comm'n v. United States Steel Corp., Docket No. 760, 2 *Statement of Case* 639 (1924).

[3] J. M. SWANK, THE MANUFACTURE OF IRON IN ALL AGES 188 (1892), quoting ISRAEL ACRELIUS, A HISTORY OF NEW SWEDEN 169 (1874).

attended. . . . It was . . . agreed to require each firm in this association to deposit a specified sum of money . . . to be used as a forfeit, in case the depositing firm is detected in cutting rates. *The equalizing of railroad freights is in the hands of a committee who as yet have made no report.*" (Italics supplied.)

The trade journals of 1875 to 1880 indicate that several groups of locally separate steel mills seeking to avoid price competition experimented with various plans of zone prices and freight equalization. In 1880 the four manufacturers of steel beams (the Carnegie Company in Pittsburgh and three others in Eastern Pennsylvania and New Jersey) formed an association for fixing prices and established Pittsburgh as the common base for quoting prices.[4] This agreement on the part of the locally separate steel beam producers to quote the Pittsburgh price plus the rail freight from Pittsburgh to destination, regardless of the actual origin of shipments or the actual freight cost incurred, appears to have been the first use of the basing point system in the United States.

In 1894 the manufacturers of nails adopted the Pittsburgh-Plus formula for the pricing of their product. According to a report of the Federal Trade Commission, "Early prices [for nails] were made mill prices, but as the business developed, manufacturers of wire and cut nails based quotations on the price f.o.b. Pittsburgh, either in carload or less than carload lots. That price at all other points was the same, with freight from Pittsburgh added."[5]

Pools, associations, and "loose-knit" combinations provided an effective means for avoiding price competition as long as business conditions were good. When demand began to decline, however, small and financially weak producers usually "broke away" and reduced their prices in order to find a selling outlet for their products.[6] When the price agreements collapsed, competition typically became ruthless and cutthroat. The larger concerns, especially, cut prices sharply in areas of active competition in an effort to coerce or discipline firms showing a price independence. Such price cutting proved to be highly chaotic because the larger concerns could usually make up some or all of their losses elsewhere. The depression of 1896-1897, it is reported, led to a collapse of all of the various pools and price associations, and the resulting price rivalries became particularly severe and demoralizing.

The weakness of pools, associations, and other forms of concerted action based upon agreement led business leaders and their legal counsel to search for more effective methods of price control. The trust device proved to be an effective method for controlling competitors and avoiding price competition, but its use was challenged and subsequently condemned in the state courts as a monopolistic measure. The revolutionary action taken by New Jersey in 1889 in providing that corporations

[4] Federal Trade Comm'n v. United States Steel Corporation, Docket No. 760, 2 *Statement of Case* 638-639 (1924).

[5] 1 *id.* at 262-263. Additional data on the early use of the basing point system may be found in THE BASING POINT PROBLEM 107-108 (TNEC Monograph 42, 1941).

[6] 13 REPORT OF THE INDUSTRIAL COMMISSION 501-502 (1901).

chartered there could own and vote the stock of other corporations appeared to provide an effective substitute for the trust device, although the enactment of the Sherman Act in 1890 raised doubts about the legality of this arrangement. These doubts, however, were largely dispelled by the Supreme Court in the *Sugar Trust* case,[7] in which it was held that the Sherman Act could not be applied to a monopolistic combination of sugar refineries on the ground that manufacturing was distinct from commerce and that a combination of manufacturing plants had only an "indirect" effect upon commerce. Upon the basis of this decision, which the Court subsequently overruled, the way became clear for large business interests to form corporations to acquire a permanent and absolute ownership interest in scores of formerly independent and competing plants.

II

MERGERS AND THE FURTHER USE OF GEOGRAPHIC PRICE DISCRIMINATION

A. Cutthroat Competition

Most of the new combinations (mergers) formed during the period 1897-1903, it appears, employed some form of geographic price discrimination in their pricing policies. In a number of cases, particularly in oil, tobacco, sugar, salt, copper, lead, iron, and steel, the combinations employed "local price cutting" in one area while maintaining prices elsewhere, expressly to injure or kill off a geographically separate competitor. This practice became known as "cutthroat competition." In 1900 the United States Industrial Commission, after an extensive investigation of the methods of competition employed by the combinations, concluded that perhaps the "greatest evil" of combinations was to be found in the fact that they "cut prices to an unreasonable extent in certain localities, and even to individuals at certain times, for the sake of driving out their rivals."[8]

The shocking use of local price cutting of the cutthroat variety was vividly revealed in the evidence presented in the *Standard Oil*[9] and *American Tobacco*[10] cases decided by the Supreme Court in 1911. Upon the basis of this and other evidence, the House Committee on the Judiciary reported in 1914 as follows:[11]

> In the past it has been a most common practice of great and powerful combinations engaged in commerce—notably the Standard Oil Co., and the American Tobacco Co., and others of less notoriety, but of great influence—to lower prices of their commodities, oftentimes below the cost of production in certain communities and sections where they had competition, with the intent to destroy and make unprofitable the business of their competitors, and with the ultimate purpose in view of thereby acquiring a monopoly in the particular locality or section in which the discriminating price is made.
>
> Every concern that engages in this evil practice must of necessity recoup its losses in the particular communities or sections where their commodities are sold below cost or

[7] United States v. E. C. Knight Co., 156 U. S. 1 (1895).
[8] 1 REPORT OF THE INDUSTRIAL COMMISSION 20 (1900).
[9] Standard Oil Co. of New Jersey v. United States, 221 U. S. 1 (1911).
[10] United States v. American Tobacco Co., 221 U. S. 106 (1911).
[11] H. R. REP. No. 627, 63d Cong., 2d Sess. 8-9 (1914).

without a fair profit by raising the price of this same class of commodities above their fair market value in other sections or communities.

Such a system or practice is so manifestly unfair and unjust, not only to competitors who are directly injured thereby but to the general public, that your committee is strongly of the opinion that the present antitrust laws ought to be supplemented by making this particular form of discrimination a specific offense under the law when practiced by those engaged in commerce.

B. Sporadic or Anarchic Discrimination

Some of the combinations were less ruthless in their pricing practices and adopted a moderate sort of discriminatory pricing "to meet competition." Products were usually sold f.o.b. the shipping mill, but at certain points in distant areas prices were cut to match or undercut somewhat the prices of a geographically separate rival. Various combinations found that a limited form of local price cutting was a profitable practice because it enabled them to avoid reducing prices in their area of freight advantage while "reaching out" to sell in distant regions. They also found that the practice was an advantageous method for checking the growth of distant rivals. When new competitors developed at certain points, delivered prices could be cut in those areas to prevent the rivals from becoming bigger and stronger competitors. This method of pricing appears to have been used by a number of combinations prior to the formal adoption of a policy of *cooperative, systematic* price discrimination.

Discriminatory price cutting to limit a competitor rather than to annihilate him has become known as "sporadic" or "anarchic" discrimination. The purpose of a dominant seller in employing this form of geographic price discrimination is largely opportunistic—that is, to charge high prices where competition is weak or non-existent and to reduce delivered prices where rivals are active. The practice is unsystematic and anarchic, and discrimination is exercised in accordance with no principle except the ambiguous one of "meeting competition." A small producer can never be sure about the delivered price quotations which he is likely to find in his local area or the extent to which they may be cut.

C. Cooperative, Systematic Price Discrimination

The problem of formulating a price and sales policy for a considerable number of geographically separate mills in the iron and steel industry was squarely faced in 1901 by those in charge of the newly formed United States Steel Corporation—the largest and most extensive of the early mergers. If the Corporation had adopted identical f.o.b. mill prices at its separate mills, the unequal freight costs to consuming centers would have given certain mills a substantial sales advantage over others. The desire of the Corporation was to eliminate price competition among its constituent plants and at the same time permit considerable local autonomy in their management. Some method, therefore, had to be found for equalizing the element of freight. In discussing the adoption of the Pittsburgh-Plus system by the Corporation

for use by its locally separate plants, Charles M. Schwab testified in 1901, "I don't see any other plan of doing it; you must establish some central point."[12]

The problem which a central financial unit has in unifying the sales policies of its constituent companies has been noted by a number of economic and legal authorities. Walter B. Wooden, a long-time student of basing point pricing, explains the situation as follows: "The full advantages of chain production are dependent upon the chain's maintenance of a system of pricing that reduces undue conflict between its own plants variously located. Such conflict would arise if the buyers were permitted to get their goods at a lower cost from one plant of the chain than from another. To permit that creates a tendency toward price competition among members of the family group that was established to avoid it."[13]

A further policy question before the Corporation was that of its relations with the remaining independents in the steel industry. There is abundant evidence to indicate that if one of the concerns in a sales area is a local enterprise while the other is a chain producer, geographic price discrimination tends to produce either (1) a condition of monopolistic exclusion or (2) a condition of cooperative, monopolistic pricing based upon conspiracy or price leadership and price following. If a local seller quotes a low price in his area of freight advantage, the multiple-plant company may retaliate and quote a lower discriminatory delivered price; and the resulting price cutting *in that area* may thereupon become cutthroat. The dominant concern is usually in a position to make up its losses elsewhere while the single-plant firm has no such opportunity. Inevitably, the local concern is faced with the prospect of being slowly or rapidly driven out of business or compelled to follow the price leadership of its more powerful rival. Historical records indicate that the Steel Corporation decided upon a monopoly policy of *including* its competitors rather than the usual one of excluding them, provided that they would follow its price leadership.

Thus it was that the regular and consistent use of the basing point formula by the United States Steel Corporation served the purposes (1) of insuring the quotation of identical prices by all mills—its own mills as well as independents—and (2) of avoiding the geographic and automatic allocation of sales which identical f.o.b. mill pricing would create. The prices announced by the Corporation at Pittsburgh became the "official" prices, and all producers quoted the Pittsburgh base prices plus the rail freight from Pittsburgh to the point of delivery regardless of their own individual location or the actual freight cost incurred.[14]

An interesting account of the establishment of the basing point system of deliv-

[12] 13 REPORT OF THE INDUSTRIAL COMMISSION 469 (1901).

[13] Wooden, *The Defense of Delivered Price Systems*, 15 GEO. WASH. L. REV. 1, 31 (1946).

[14] A detailed record of the part played by the United States Steel Corporation in establishing the use of the basing point system for the sale of all steel products except rails may be found in Federal Trade Comm'n v. United States Steel Corporation, Docket No. 760, *Statement of Case*, Brief and Argument by Attorneys for the Federal Trade Commission, and Trial Examiner's Report on the Facts (1924).

ered prices in the sale of bars and plates is contained in the following report written in 1901 by a trade correspondent in Philadelphia:[15]

Early in the year it looked as though there might be a somewhat demoralized market for bars and plates, but this was fortunately avoided by the manufacturers of each of these specialties formulating plans for maintaining uniform prices, which have proved to be eminently successful. It took a good deal of time to arrive at a basis which would be satisfactory to all the various interests, one great difficulty being in the variety of conditions in regard to location of mill, proximity to markets, cost of production, etc. The plan finally adopted and which has worked perfectly so far, and which is likely to be continued indefinitely, was to base all quotations at a figure agreed upon for f.o.b. deliveries in Pittsburgh. The local mills (Philadelphia) therefore quote Pittsburgh prices—plus freights to whatever point the material has to be shipped. . . . The same plan is in force among the plate mills, although it is less binding than that in bars. The plate mills have a verbal agreement, and the bar mills have a written agreement which is further strengthened by a substantial cash deposit. The lowest prices during the year were $1.35 for bars and $1.40 for plates, but under the price agreement they are now $1.62 and $1.72, and likely to remain at that for an indefinite period.

Shortly after the general adoption of the basing point plan in the iron and steel industry in 1901, the practice was extended to the cement industry.[16] Thereafter, the plan had little vogue until around 1912 when its use became widespread. Products, in addition to iron and steel, which came to be sold on a *single* basing point plan were cast-iron soil pipe, glucose, malt, maple flooring, welded chain, zinc, lead (St. Louis plus freight differentials), and copper ("Connecticut Valley" plus freight differentials). Certain industries adopted a *multiple* basing point system in which two or more basing points were established by industry leaders for pricing purposes. Representative products which came to be sold on a multiple basing point plan were cement, iron and steel (after 1924), hardwood lumber, gasoline, sugar, chemical fertilizers, milk and ice cream cans, asphalt roofing materials, linseed oil, rigid steel conduit, fire brick, lubricating oil, and plate glass.

III

THE BASING POINT FORMULA

A. A Form of Cooperative, Systematic Price Discrimination

The essence of the basing point formula (in contrast with f.o.b. mill pricing) is the sale of goods at delivered prices which are determined by quoting the base price of *some other* mill plus freight from *that mill* to destination. In so far as a mill quotes its own mill price, uniform to all customers, it is engaging in f.o.b. mill pricing. Basing point pricing comes into existence when geographically separate

[15] THE PHILADELPHIA IRON MARKET FOR 1901, ANNUAL REVIEW OF THE NEW YORK METAL EXCHANGE 3 (1902).

[16] FTC, PRICE BASES INQUIRY: THE BASING POINT FORMULA AND CEMENT PRICES 29-41 (1932). In 1948 the Supreme Court held that the Federal Trade Commission was fully justified in finding "understanding expressed or implied" in the establishment and use of the multiple basing point system in the cement industry. Federal Trade Comm'n v. Cement Institute, 333 U. S. 683, 716 (1948).

mills quote delivered prices for any destination by adding to an established base price at a given point, called the basing point, the freight charge—usually rail freight—from that point to the point of delivery, regardless of the actual origin of shipments or the actual freight cost incurred. As a general rule, it may be said that the selection of a base price is made by a price leader (a dominant corporate merger).[17] The base price or prices so established are thereupon accepted (with rare exceptions) by all other mills for making sales in the contiguous territory.

The various mills in a basing point industry may employ one or more bases for the entire country, and in some industries every mill may serve as the base mill for its contiguous territory. The practice of charging a customer the freight cost which he would pay in getting delivery from a nearer supplier rather than the seller's actual transportation cost, is known as freight equalization. In a plan of freight equalization every mill is usually regarded as a base.

The price relationships which arise in multiple basing point selling are illustrated in Fig. 1. A, B, and C, it may be assumed, are sugar mills selling in their own localities, as well as in the principal consuming center of B. A and B are base mills, and C is a non-base mill. Under the multiple basing point system each seller quotes

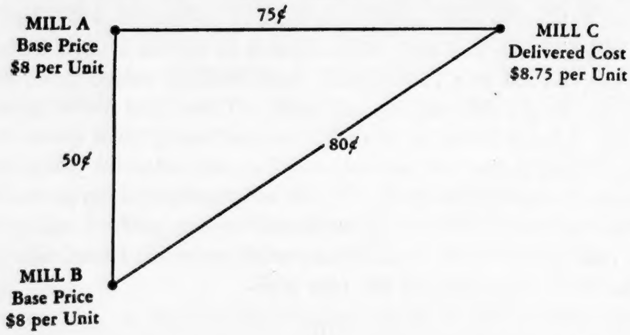

FIG. 1. The multiple basing point system of delivered prices. All mills regularly quote the particular "base price" plus freight from the basing point to the customer's location which gives the lowest combination of base price and freight cost. The essence of the basing point plan is the use of the base price and freight of some other mill.

a delivered price which is the lowest combination of a base price at any base mill plus the rail freight from that mill to a particular destination. Thus all buyers at C are given an identical delivered price quotation of $8.75 per unit. Mill C, it may be noted, charges its local customers a freight item of 75 cents per unit which it does not pay out in making delivery. This fictitious charge is known as "phantom freight." Phantom freight may be defined as the excess of the freight item charged the buyer over the freight actually paid out by the seller in making delivery. The "justification" which business interests usually give for phantom freight is the asser-

[17] Brief for Respondents, Vol. I, App. A, pp. 474-476; Federal Trade Comm'n v. The Cement Institute, 333 U. S. 683 (1948).

tion that the price of \$8.75 per unit is the price which a buyer at C would have had to pay for sugar if someone had not chosen to build a factory at C.

On sales in B all buyers are given an identical delivered price quotation of \$8.00 per unit. This pricing practice means that mills A and C have their mill net prices reduced 50 cents and 80 cents respectively by "freight absorption." Freight absorption is defined as the excess of the actual freight paid in making delivery over the amount of the freight item used in calculating the delivered price.

The absorption of variable amounts of freight on current sales (as well as the charging of variable amounts of phantom freight) results in variable mill net prices. In the *Staley* case[18] price discrimination was considered by the Supreme Court to be the making of a difference in the net amount charged to different buyers by any seller. This view of discrimination is in accord with the concept of discrimination employed in economic analysis. The price discrimination involved in the basing point system was said by the Court to be *regular* and *systematic*. The discrimination is regular and systematic because (1) all geographically separate mills regularly quote the delivered price of the appropriate base mill and (2) they absorb (or add) just enough freight (no more and no less) to match the base price plus the rail freight from the basing point to the customer's location.

B. The Exclusion of Independent Merchants and Distributors

The adoption of basing point pricing has involved the use of two additional restrictive sales methods. A consideration of these factors, unfortunately, has largely been overlooked in current discussions of the basing point problem. The first is the concerted practice of basing point mills to refuse to sell to independent merchants and distributors. In their efforts to manage prices the large combinations soon found that supplies in the hands of middlemen and dealers directly limited their power to raise prices as consuming demands increased. Independent merchants typically accumulated large inventories of basic commodities—such as pig iron, merchant bars, copper, lead, and zinc—during periods of low prices and slack demand, for sale when fabricating industries resumed their buying. This activity helped to maintain an even state of employment and production. The combinations, however, found that the presence of accumulated supplies in independent hands not only limited their ability to get higher prices during a period of business expansion, but also provided a source of competition over which they had no control.

In order to eliminate the troublesome competition of independent distributors, all of the large steel producers soon after 1901 opened their own district sales offices and assumed an almost complete control over the distribution of their iron and steel products. Local jobbers were permitted to stock a few products—such as horseshoes, nails, galvanized sheets, and fencing—for local sale and usually at prices higher than the delivered carload rate. Such jobbers, however, were sold only a few carloads at a time, and speculative buying was not permitted.

[18] Federal Trade Comm'n v. A. E. Staley Mfg. Co., 324 U. S. 746, 751 (1945).

The combinations in the non-ferrous metals industry similarly sought to strengthen their use of basing point pricing by adopting the policy of selling only to consumers (fabricators). Soon after 1901 the lead combination adopted the policy of selling refined and common pig lead only to consumers, and in quantities which it believed they should purchase. This industry policy has been continued to date. The primary producers of copper likewise adopted a general policy of refusing to sell to dealers or speculators. Their declared reasons for this policy are (1) to discourage trading on the commodity exchanges and (2) to prevent dealers from acquiring supplies for sale again when consumer demands are rising.[19] In a program of stabilizing zinc prices, the major zinc producers in 1928 established East St. Louis as the basing point for Prime Western slab zinc and uniformly restricted sales of zinc to consumers.[20]

In the development of the cement industry the usual marketing policy was one of selling through distributors and other wholesale middlemen at f.o.b. mill prices. A witness for the industry in the recent *Cement* case, for example, stated, "In the early days of the distributor relationship the sales were at f.o.b. mill prices. The commitments from the distributors to ourselves were definite commitments and the distributor was at perfect liberty and did sell as he could, for whatever measure of profit he could get."[21] The elimination of the independent merchants in the cement industry, and the discontinuance of making all sales f.o.b. the mill took place in various regions from 1902 to 1912.[22] As in the case of iron, steel, and the non-ferrous metals, the elimination of the cement merchants by a combination or industry group occurred quite abruptly. An industry witness in the *Cement* case, for example, testified, "We eliminated most of them at the end of 1902."[23]

The results of "fencing in" the demand for iron and steel, the non-ferrous metals, and many other basic commodities have been more far reaching than is generally realized. Merchants and speculators bought supplies when consumer demand was declining and sold them again when business improved. This activity helped to provide first-hand producers with a continuous market and also served to stabilize prices. In restricting the sale of their products to fabricators, processors, and local jobbers, the large combinations have created a condition in which there is little, if any, current demand whenever the consuming industries are not buying. The demands of consuming industries, moreover, are usually quite irregular, for they reflect the variable demands of ultimate consumers and the general state of business. By "fencing in" the demands for their products, basing point industries have accentuated the problem of providing sustained employment and production.

[19] *Hearings before Temporary National Economic Committee on P. Res. 113*, Pt. 25, 76th Cong., 3d Sess. 13244-13245 (1940).

[20] VERNON A. MUND, OPEN MARKETS 199-201 (1948).

[21] Brief for Appellants, Vol. I, App. A, p. 105, The Cement Institute v. Federal Trade Comm'n, 144 F. 2d 221 (C. C. A. 7th 1945).

[22] *Id.* at 104-115.

[23] *Id.* at 111.

In 1899 the tin-plate workers of Pittsburgh called attention to the serious impact on employment of the newly established policy of the tin-plate combination to restrict sales to consuming buyers of its own choice. According to the union, "When the trade was in the hands of independent firms, large quantities of ware were manufactured into stock against future calls or sold at very small profits to large buyers who stocked it in their own warehouses against the brisk season; thus the workmen were given employment throughout the slack winter months. But the trust, having complete control of the trade, will neither incur the cost of storage on its own premises nor abate its ironclad prices so that the buyers may lay up a stock for future trade."[24]

C. Price Management and the Curbing of Production

A second restrictive policy which the large combinations adopted in conjunction with basing point pricing was that of producing only those quantities which could be sold at the managed prices. The general practice of independent mills prior to the formation of monopolistic mergers was to produce continuously, in good times and bad, for sale to a variety of trade interests—merchants, speculators, fabricators, and industrial users. When the level of business activity declined, it was the inefficient, poorly located mills which discontinued their operations. At no time, it appears, was there a general curtailment of production by *all* mills—efficient and inefficient. With the formation of mergers, however, the production of all mills was typically curbed to prevent an accumulation of supplies and a "breaking" of prices. The large combinations could and did sharply restrict the output of their own mills, and the remaining independents soon adopted a similar policy. Since the established plan was one of refusing to sell to nonconsuming interests, a producing mill either had to find customers at the "official" prices or store its products in its own warehouses. Most mills did not—and do not—have large storage facilities. The practical alternative, therefore, became one of restricting output and employment rather than of producing for inventory.

The hearings of the Federal Trade Commission on basing point pricing in the cement industry showed clearly that the limited storage facilities possessed by first-hand producers are a barrier to continuous employment. Industry members repeatedly stated that the storage facilities of most plants are insufficient for continuous production.[25]

IV

THE FREIGHT ALLOWED OR ZONE DELIVERED PRICING SYSTEM

A. History and Operation

A second type or form of delivered pricing is the "freight allowed" or "zone delivered" method of price quotation. When this method of pricing is used jointly

[24] 1 REPORT OF THE INDUSTRIAL COMMISSION 905 (1901).

[25] Brief for Appellants, Vol. I, App. A, p. 79, The Cement Institute v. Federal Trade Comm'n, 144 F. 2d 221 (C. C. A. 7th 1945).

by two or more sellers (either by agreement or by price following), it also results in identical delivered prices and an avoidance of price competition.

The first use of the freight allowed method of pricing appears to have come with the formation of the American Tobacco Company in 1890. During the period 1890 to 1900 the plan was extended to the sale of such products as water meters, wire rope, retail scales, meat slicers, and meat choppers. From 1900 to 1904 pipe tools, vises, pipe cutters, auger bits, wood boring tools, screw drivers, and machine knives were priced "freight allowed." From 1908 to 1912 the practice was adopted by manufacturers of automobile tires, tire chains, brake lining, various chemical products, and electric lamps. Many additional industries adopted freight allowed methods of selling during the National Recovery Administration (1933-1935), and new applications have been made up to the present time.

In using the freight allowed method of pricing, a seller quotes a base or zone price containing an average freight item and thereupon "allows" the freight from his mill to destination. The goods may be sent prepaid or the buyer may be directed to pay the freight and deduct it from the invoice cost before remitting payment. In certain cases, the practice is for a seller (or industry group) to establish a national uniform delivered price applicable to any established freight station in the United States. This is the basis on which the Post Office Department carries the mail. In other cases the country is divided into two or more geographical areas or zones, and a uniform delivered price (including a transportation increment averaged for the zone) is quoted for each zone.

A classification of the various methods of selling products "freight allowed" may be made as follows:[26]

1. *Goods sold at one list or base price for the entire country with a full allowance of freight to any established freight station.* A minimum shipment may or may not be specified. Examples of products sold by this method include—

Arc Welding Machines
Tire Chains (24 pairs)
Brake Lining (100 lbs.)
Multi-blade Fans, Blowers, and Air Washers
Household Electrical Appliances
Files and Rasps (150 lbs.)
Machine Knives
Rubber soled Canvas Footwear (100 lbs.)
Lubricated Plug Valves (500 lbs.)
Steel Split Pulleys
Copper Wire (insulated or plain), Cable, Sheets, and Tubing (200 lbs.)
Brass and Bronze Wire or Cable (200 lbs.)
Mechanics' Hand Tools
Flexible Steel and Aluminum Conduit (100 lbs.)
Bakelite
Rubber Fuel Tanks
Rubber Cement
Aluminum Products (500-1,000 lbs.)
High-grade Zinc
Mechanical Rubber Goods (100 lbs.)
Leather Transmission Belting (100 lbs.)
Steam Condensors (traps)
Sheet Metal Fittings ($200)
Asbestos Products
Water Meters (150 lbs.)
V-Drive Pulleys and Belts (100 lbs.)
Pneumatic Tools and Hoists
Stillson Pipe Wrenches (200 lbs.)
Air Compressor Hose (500 ft.)
Rubber and Fabric Transmission Belting (100 lbs.)
Chain Hoists (Hand operated), Trolleys, and Winches (100 lbs.)
Marine Specialties and Ship Fixtures (100 lbs.)
Soft Drinks

[26] The examples of products sold at zone delivered prices are from a survey made by the writer in 1949. This survey was undertaken for a forthcoming book, *Government and Business*, to be published in the spring of 1950.

2. *Products sold at one list or base price for the entire country with "freight allowed and prepaid" to any established freight station.* Representative products sold by this method include—

Cadmium
Industrial Motors and Controllers
Electric Lamps (standard packages)
Biologicals, Arsenicals, Insulin, and other drug specialties
Coated Abrasives (200 lbs.)
Rubber Covered Building Wire
Cable Accessories and Magnet Wire (100 lbs.)
Dictating Machines and Accessories
Typewriters
Glazier Tools (100 lbs.)
Groceries; Trade-marked items—such as soap, canned soup, shortening, cereals, cake flour, and canned dog food (1 carload)
Automobile Tires and Tubes (200 lbs.)
Cash Registers, Accounting Machines, Adding Machines, and Check Writing Machines.
Notions—such as zippers, buttons, pins (Variable minimums)
Cotton Thread (100 lbs.)
Cigarettes and Tobacco Products
Candy Bars (100 lbs.)

3. *Products sold to dealers and industrial users with "freight allowed" or "allowed and prepaid" within zones.* Representative products include—

Arc Welding Electrodes (100 lbs.)
Hard Fiber Twine
Insulating Board Products
Water Works Valves
Scales, Meat Choppers, Slicers, and Coffee Mills
Power Cable
Street Lighting Equipment, Reactors, Feeder Regulators (100 lbs.)
Distribution Transformers
Portable Air Compressors
Portable Elevators
Glass Containers
Brass and Copper Strip (100 lbs.)
Paint
Screws, Nuts, Bolts
Electric Grinders
Gasoline Service Station Pumps
Lubricating Oil, Grease, and Kerosene Dispensing Equipment
Hydraulic Lifts (Gasoline Station)
Sash Pulleys (100 lbs.)
Folding Chairs and School Chairs
Chain, Sprockets, Gears, and Power Transmission Machinery (100 lbs.)
Wire Rope (200 lbs.)
Liquid Chlorine
Feed Water Heaters
Cross Cut Saws and Handles, Hack Saw Blades and Frames, Hand Saws, and Saw Tools (100 lbs.)
Lye
Hand Lift Trucks
Paper Bags
Water Softeners

4. *Products sold to local jobbers and distributors with freight allowed to designated distribution points.* Representative products include—

Portable Electric Tools (100 lbs.)
Various Chemical Products
Air Rifle Shot (200 lbs.)
Oil Cans, Oilers, Fillers, and Torches
Electric Fans (100 lbs.)
Plumbing Fixtures (carload lots)
Ammunition
Kraft Paper and Kraft Container Board
Firearms (100 lbs.)
Dry Cell Batteries and Flashlights (200 lbs.)
Pliers, Wrenches, and Small Tools (100 lbs.)
Rock Drills (100 lbs.)
Auger Bits, Wood Boring Tools, and Screw Drivers ($100)
Manila Rope (200 lbs.)
Road Machinery
Ladders
Brass and Copper Products

B. Reasons for the Use of the Freight Allowed Policy

The freight allowed method of price quotation may be used independently and individually by a given seller for any one of a number of reasons. Some sellers report that they desire to have a uniform national retail price for advertising purposes and at the same time give their variously located retailers the same delivered cost. This is accomplished by including an average freight item in the quoted price. Other manufacturers report that they desire to place their wholesale distributors in adjoining territories on "an equal competitive basis." Some firms state that they employ a zone pricing system in order to secure lower delivered costs on sales into distant

areas. By averaging the freight item, the seller can hold delivered costs in other areas to a lower level.

Although zone delivered pricing methods may be used independently, the evidence indicates that they are often employed by an entire industry group. With the systematic practice of full freight allowance and with identical factory (or base) prices, the plan serves as an effective method for securing identical delivered prices. Each locally separate seller simply adopts the base or zone price announced by the dominant seller or sellers with the proviso "freight allowed" or "freight allowed and prepaid," and all buyers at a given destination point are thereupon given the same quotation. (See Fig. 2.)

$1.00 Freight

MILL A	MILL B
Base or Zone Price $20	Base or Zone Price $20
(Freight Allowed)	(Freight Allowed)

FIG. 2. The freight allowed or zone delivered system of pricing. Each seller following the formula adopts an identical base or zone price (containing an average freight item) and "allows" the freight from his mill to the destination. Buyers at all destination points, accordingly, are given the same price quotation.

V

PRACTICES USED BY DOMINANT SELLERS TO SECURE THE OBSERVANCE OF DELIVERED PRICING FORMULAS

During periods of declining demand, independent mills (usually single plant competitors) are frequently tempted to deviate from the use of delivered pricing formulas on sales in certain areas or to certain customers in an effort to secure an outlet for their products. There is abundant evidence to show that the price leader (or leaders) usually takes immediate steps to correct this situation. One method used is to talk with the recalcitrant mill about the dangers of sporadic and cutthroat discrimination. The general counsel for the United States Steel Corporation, for example, has advised his client that "The harmful effects of cutthroat competition, of unfair trade methods, of selling below cost or even a fair margin of profit, and the like, are legitimate subjects of discussion."[27] The fear of discriminatory pricing practiced by large concerns is still a powerful motive which serves to secure and maintain compliance.

A common method employed by industry leaders to maintain the observance of basing point systems is that of imposing a "punitive base price" on the competing mill which is equal to the lowest mill net price received by the competing mill. In using this technique, a price leader quotes a low base price in the area of the rival

[27] *Hearings before the Temporary National Economic Committee*, Pt. 20, 76th Cong., 2d Sess. 10994 (1939).

mill to govern all sales made in that area. This practice means that the low price made by the rival mill for a few sales will prevail on *all* local sales.[28]

Another practice employed by an industry leader to secure compliance with delivered pricing systems is that of "price raiding." Price raiding means the "cutting" of delivered prices in particular local areas, or to particular customers, usually in a discriminatory way, expressly to injure the concern showing a price independence. The resulting price chaos is known as a "price war." The power of a dominant concern to cut prices to extremely low levels is based either upon financial strength or upon the existence of monopoly power in certain areas in which the losses may be recouped.[29]

The privilege of using discriminatory pricing methods (especially sporadic geographic discrimination) gives industry leaders a powerful weapon of coercion and discipline for securing unity of action on price. A further factor accounting for unity of action is the extra profits which all sellers may secure through an avoidance of price competition. As a result of the factors of fear and favor, every follower acts in a restrained manner as if he were forbidden to reduce the delivered prices required by the industry formula. Upon the basis of this consistent mutuality of behavior, various economists, the Federal Trade Commission, and the courts have concluded that the collective or parallel use of basing point or zone delivered pricing systems involves either agreement or a mutual restraint on individual action with illegal trade restraining effects.

VI

DELIVERED PRICING SYSTEMS AND INDUSTRIAL DECENTRALIZATION

Basing point and zone delivered pricing systems operate not only to eliminate price competition, but also to prevent a decentralization of industry. The use of an eastern base price makes for high cost-prices in the West and South and discourages the development of local fabricating industries. Local fabricators which do develop, moreover, cannot ship eastward to any significant extent in competition with fabricators located near an eastern basing point, because the delivered costs of their basic supplies are higher.

When basic products (such as aluminum) are produced in the West and South and sold "freight allowed," the development of local fabricators is likewise restricted. Local prices are high—as high as elsewhere in the country—and fabricators find no cost advantage in building plants near the sources of supply. The sale of fabricated products (such as copper wire, cable, and tubing) by eastern mills at freight allowed prices (based upon an average freight item) also serves to discourage the develop-

[28] Data on the use of punitive base prices to discipline industry members showing a price independence may be found in Brief for Appellees, Vol. I, App. A, pp. 495, 499, 504-505, Federal Trade Comm'n v. The Cement Institute, 333 U. S. 683 (1948).

[29] Corwin D. Edwards cites the case of a large producer in the building materials industry which has carried a cash reserve of over 10 million dollars for use as a "war chest" to discipline rivals who reduce prices below levels which the company regards as satisfactory. EDWARDS, MAINTAINING COMPETITION 169-170 (1949).

ment of distant fabricators, for the established mills, in effect, are able to "dump" into the distant areas by absorbing some or all of the freight—at the expense of their nearby customers.

VII

SOME CONCLUSIONS ON THE USE OF BASING POINT AND ZONE DELIVERED PRICING SYSTEMS

Historical data show that with the rise of markets in the American economy, industrial and agricultural products were typically sold at f.o.b. prices. Subsequently, with the rise of mergers, basing point and zone delivered pricing systems were increasingly adopted by multiple-plant producers in order (1) to insure identical delivered prices and (2) to avoid the automatic allocation of sales which f.o.b. mill pricing would involve. In general, independent producers were given the opportunity of following the leader on price. A policy of price following was usually adopted in order (1) to secure extra profits or (2) to eliminate the instability of sporadic discrimination. Delivered pricing systems were widely adopted during the period of the National Recovery Administration when the application of the anti-trust laws was suspended.

Basing point and zone delivered pricing systems are only two of several special devices of restriction employed by monopolistic groups. Other important and concomitant devices are (1) the concerted refusal of organized producers to sell to independent dealers and distributors and (2) the curbing of production to those quantities which can be sold at the managed prices.

Basing point and zone delivered pricing systems work an injury to buyers because (1) they force some buyers to pay an overcharge for freight; (2) they deny all buyers the privilege of arranging for the purchase of their own transportation; and (3) they usually result in an elimination of independent price competition.

Local price cutting—cutthroat and sporadic—is a principal means by which dominant firms coerce, injure, and discipline geographically separate independents. At the present time, the use of cutthroat competition has largely been replaced by that of sporadic or anarchic discrimination practiced to limit a competitor rather than to destroy him.

Spokesmen for big business frequently attempt to justify sporadic price discrimination by declaring that this method of pricing promotes competition. In absorbing all or a part of the freight charges, it is said, sellers can acquire business in distant markets and buyers are given a wider choice of sellers. The fact is, however, that sporadic discrimination is only a *limited* kind of competition—restricted to certain areas. It is not the kind of competition found in open markets.

Experience has shown, moreover, that sporadic discrimination usually works to the disadvantage of small, single-plant competitors. When a small business firm is getting established in a particular area, it frequently finds that it must offer its goods at prices somewhat below those of a large rival. Its prestige and reputation are not

firmly established, and some inducement must be offered to secure customers. If a large distant concern is permitted to match the local prices by reducing its mill net prices on sales in that area, the small rival may have little opportunity of ever developing its business.

Neither economists nor lawyers have thus far been able to develop a workable rule or standard for use in permitting the exercise of freight absorption, except by reference to the exclusion of competitors. Where can the line be drawn between legitimate and illegitimate degrees of geographic price discrimination? Must an efficient producer wait for relief until he has been forced into bankruptcy? If a mill shrinks its mill net to ship into a distant area and regularly matches the price which it finds, it is following a plan of *systematic price discrimination*. This is the monopolistic basing point practice. On the other hand, if a mill quotes a discriminatory delivered price which is below that of a rival in the distant area, it is a case of *local price cutting* which Section 2 of the Clayton Act was expressly designed to prevent.

There is no logical basis for legalizing price discrimination which is exercised "in good faith to meet competition." As applied to geographic price discrimination, the term "meeting competition" means the cutting of net prices to buyers *in a certain area* while maintaining them on sales made in other areas. Meeting competition, in this sense, is the very act of discrimination. In real markets (local, central, or primary), sellers do not "meet competition" by engaging in price discrimination.

The phrase "*in good faith* to meet competition" has no established or generally accepted economic or legal meaning. A consideration of "motives" is a task for mind readers and clairvoyants rather than for administrative agencies and the courts. All business is done for commercial advantage; and the task of supervising a policy of legalized geographic price discrimination would impose an exceedingly difficult burden upon the antitrust agencies.

An important reason for going further in the direction of required f.o.b. mill pricing is to try to get behavior which is like that found in competitive markets. With the collective use of basing point and zone delivered pricing systems, sellers do not have a motive—a competitive pressure or compulsion—to reduce base prices in order to provide a selling outlet for their capacity. When business begins to decline, a basing point or freight allowed practitioner reaches out for customers by absorbing larger amounts of freight. The extent to which he reduces his mill net by absorbing freight depends upon how "hungry" he is for business. As a result of this practice, a seller secures lower net prices on a part of his sales, but delivered prices to buyers are usually not reduced. An abolition of freight absorption would do much to correct this situation. Locally separate mills would be provided with a genuine motive to reduce their base prices in order to sell in distant consuming areas, and the resulting price flexibility would insure a more rapid adaptation of the economy to changes in the conditions of demand and supply.

F.o.b. mill pricing is only a partial remedy for the problems of geographic price discrimination and identical delivered pricing, for the factors of collusion, conspiracy, and monopolistic mergers still remain. If the substance of the problem of industrial monopoly in the United States is to be reached, consideration must be given to centralized financial control and corporate concentration.[30]

[30] See, particularly, the remedies proposed by Corwin D. Edwards, *id.* at 133-155.

THE ECONOMICS OF BASING POINT PRICING

GEORGE W. STOCKING*

Basing point pricing, adopted by steel producers some fifty years ago and since by many other industries, has been a subject of vigorous controversy among lawyers and economists for a quarter of a century. The clash of views has raised temperatures to the point of incandescence and has eventually shed some light on an intricate and significant problem. In the light, all economists have not seen the problem alike, but they have lined up on opposite sides of an issue, the general nature of which is fairly clear. That issue is whether basing-point pricing results from independent decision-making by business rivals, each anxious to maximize his earnings, or from conspiracy. A parallel issue is: what should be done about it? The second issue has forced students to look at the economic consequences of basing point pricing as well as its causes. Moreover, as the controversy has sharpened the issues, it has also narrowed the differences. Thus it has made for intellectual progress.

I

CONSPIRACY V. SPONTANEOUS EVOLUTION

The late Frank A. Fetter, Vernon Mund, and Fritz Machlup have been the most articulate "members" of what may be called the "conspiracy school."[1] John Maurice Clark has been by all odds the most articulate proponent of what may be called the doctrine of "spontaneous evolution." He has found strong allies in Melvin G. de Chazeau, Theodore Yntema, and Arthur Smithies.[2]

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[1] *Cf.* FRANK A. FETTER, THE MASQUERADE OF MONOPOLY (1931); *The New Plea for Basing-Point Monopoly*, 45 J. POL. ECON. 577 (1937); *Exit Basing Point Pricing*, 38 AM. ECON. REV. 815 (1948); VERNON MUND, OPEN MARKETS, esp. 165 ff. (1948); *Monopolistic Competition and Public Price Policy*, 32 AM. ECON. REV. 727 (1942); *Application of Economic Analysis to Antitrust Law Policy*, PROCEEDINGS TWENTIETH ANNUAL CONFERENCE OF THE PACIFIC COAST ECONOMIC ASS'N 75 (Dec. 1941); *The "Freight Allowed" Method of Price Quotation*, 54 Q. J. ECON. 232 (1940); FRITZ MACHLUP, THE BASING-POINT SYSTEM (1949).

[2] Clark, *Basing Point Methods of Price Quoting*, 4 CAN. J. ECON. AND POL. SCI. 477 (1938); *Imperfect Competition Theory and Basing-Point Problems*, 33 AM. ECON. REV. 283 (1943); *The Law and Economics of Basing Points: Appraisal and Proposals*, 39 AM. ECON. REV. 430 (1949); *Machlup on the Basing-Point System*, 63 Q. J. ECON. 315 (1949). I MELVIN G. DE CHAZEAU, CARROL R. DAUGHERTY, AND SAMUEL S. STRATTON, THE ECONOMICS OF THE IRON AND STEEL INDUSTRY 533-578, esp. 537 (1937). De Chazeau concludes that although in the beginning rivals cooperated in establishing and maintaining the basing point system, the underlying technological characteristics of the steel industry, plus the formation of the United States Steel Corporation in 1901, "made it certain that a basing-point system of prices would be adopted for rolled products." *Id.* at 537. He also states that "agreement is not a necessary condition of uniform pricing under oligopoly." II *id.* at 631.

Each of these two groups has a logical theoretical basis for its position. The conspiracy school—particularly Fetter and Mund—relies largely on the logic of competitive pricing; the spontaneous evolutionary school, on the logic of oligopolistic pricing.[3] Neither group rejects wholly the logic of the other; they differ in applying it to somewhat obscure industrial facts.

A. The Logic of the "Conspiracy School"

The conspiracy school contends that the systematic practice by business rivals of quoting delivered prices at any destination equal to the lowest combined base price and freight charge to that destination is itself evidence of conspiracy and should be prohibited by law. The implied remedy is mandatory f.o.b. pricing.[4] As stated above this conclusion is based on the logic of competitive pricing. According to this logic as expounded by Mund, no seller of a standardized product will accept less from any buyer than he can get from any other buyer; no buyer will pay to any seller more than he need pay any other seller. The rivalry of sellers, each trying to get as much as he can for what he sells, and the rivalry of buyers, each anxious to pay as little as possible for what he buys, will force all sellers to sell to all buyers at the same price in the same market. The "principle of indifference" prevents discrimination. Delivered prices will consist of the f.o.b. price plus freight to the delivery point. They will differ solely by differences in transportation costs. In competitive markets there may be several production centers which compete for business on the margin of their normal market areas. Relative production costs and transportation rates will determine the boundaries of the competing markets. These may shift from time to time in response to changes in the conditions of supply and demand. But as Mund puts it, "The prices in two different market places . . . do not differ, except temporarily, by more than transportation costs and handling charges, for competing traders will ship goods and level off the price differential."[5] According to Mund, four conditions are essential to this kind of pricing: (1) freedom of competition in trading; (2) freedom of entry; (3) a willingness by producers to compete; and (4) a market demand that warrants more than

See also United States Steel Corporation, TNEC Papers (1940), in three volumes, especially Volume III, THE BASING-POINT METHOD. Volume I, ECONOMIC AND RELATED STUDIES, states in a foreword: "The work of an economic nature was under the direction of Professor Theodore O. Yntema of the University of Chicago. He also acted as a consultant on the economic issues considered in the study of the Basing Point Method." The analysis of Volume I, ECONOMIC AND RELATED STUDIES, lends support to the de Chazeau thesis. Smithies, *Aspects of the Basing-Point System*, 32 AM. ECON. REV. 705 (1942).

[3] Clark makes it clear that he uses theory as an analytical tool. "In the last analysis the conclusive thing is not any theory as such, but an understanding interpretation of the forces actually at work in basing-point industries. In this process theories can help or mislead, according to how they are used; but they cannot be relied on for ready-made answers." *Imperfect Competition Theory and Basing-Point Problems*, 33 AM. ECON. REV. 283, 285 (1943).

[4] Although Fetter, Mund, and Machlup all apparently accept this remedy, they do not use precisely the same arguments in justifying it. In citing any one of these, I do not imply that any other occupies precisely the same position. In my judgment Machlup's is the more sophisticated logic and it is not inconsistent with the logic of imperfect competition, of which it indeed takes account.

[5] Mund, *Prices Under Competition and Monopoly: Some Concrete Examples*, 48 Q. J. ECON. 288, 299 (1934).

one producer. Mund illustrates his conception of competitive pricing by a study of the pricing of lettuce, potatoes, apples, beans, and furs in the Puget Sound area. He found that for any one of these products bought in this market all buyers, remote or nearby, paid the same f.o.b. price at any time. Because distant buyers had to pay higher transportation charges, they paid higher delivered prices. As Mund puts it, "A seller with competition . . . is effectively precluded from practicing discrimination; that is, from making a difference in prices without a corresponding difference in quality, service or conditions in the terms of sale; or from not makng a difference in prices for a difference in the service rendered."[6]

From his analysis of competitive pricing in produce markets he concludes that whenever sellers discriminate among buyers, they are monopolists. Where monopoly power grows out of location, as for example, an isolated cement plant, the monopolist sells at high prices in his "protected" territory and cuts prices to distant buyers (by absorbing freight) "to the extent that the plant desires the business or that it wishes to forestall or eliminate competition."[7] But monopolies through collusion (open or tacit) are more prevalent than single-seller monopolies, and the basing point system is a common device for strengthening such collusion. The different mill nets that sellers realize under it, being discriminatory, are evidence of monopoly.

Mund made his study of competitive pricing before the recent theory of imperfect competition had made its imprint on the thinking of economists. More recently he has taken account of the theory of oligopolistic pricing.[8] He recognizes that fewness of sellers makes collusion easier, and that small sellers through fear or avarice may choose to follow a price leader in a market where there is a dominating seller. At one point he concedes that, "Assuming strict rational behavior, identical output and trade interests, a demand that is highly inelastic, and few sellers with entry of others improbable, it is conceivable that each seller might hesitate to reduce his price for fear his rivals would follow suit." He believes such assumptions are highly unrealistic, however, and that if sellers act independently in markets in which "no one person [is] so dominant as to be able to threaten or ignore the price independence of another," competitive pricing will result. He concludes that even where only two evenly matched sellers supply a market, if they do not conspire, prices will be competitive—that is, equal to total unit cost in the long run, marginal cost in the short. In brief, to Mund, discrimination means monopoly; monopoly in markets of more than one seller means collusion; collusion means monopoly profits—that is, prices above marginal cost in the short run, with a tendency to exceed total unit cost in the long run. As he expresses it, "When sellers are few in number . . . the frequently found desire to form rings and combinations is most easily effected. The power which brings, and holds, a few rivals together is simply the cohesive

[6] *Id.* at 299.
[7] *Id.* at 301.
[8] Mund, *Monopolistic Competition Theory and Public Price Policy*, 32 AM. ECON. REV. 727, 728-730 (1942).

power of private plunder." Elsewhere he raises the question, "When *can* a concern or industry discriminate in price?" And he answers it: "It is a generally accepted economic principle that systematic price discrimination can occur only with monopoly. Thus the 'inherent' and 'structural' elements which, it is said, make possible price discrimination, can logically do so only *after* producers have secured monopoly by agreement upon a pricing formula."[9]

While Mund nowhere states his position on policy toward basing point pricing, his reasoning seems to be: (1) conspiracy is a prerequisite to the basing point system; (2) conspiracy is illegal; (3) therefore basing point pricing is illegal; and (4) it should be prohibited. Machlup and Fetter reach similar conclusions.[10]

B. The Logic of the Doctrine of Spontaneous Evolution

Chamberlin, primarily a theorist, gave a powerful weapon to policy-makers.[11] Unfortunately it has proven a double-edged sword, wielded lustily both by those who favor and those who fear Big Business. Opponents of Big Business have argued that since oligopolists behave like monopolists and since oligopoly is inevitable, the government must regulate business in the public interest.[12] Proponents have used the Chamberlinian doctrine as a defense in antitrust proceedings.[13] The essence of the Chamberlinian doctrine of oligopoly is that if only a few well-informed sellers control the sale of any standardized product and each behaves rationally, trying to maximize his earnings, he must take account of the total effect—direct and indirect—of his decisions. Recognizing that his rivals will meet his lower price if he cuts them, an oligopolist refuses to cut.[14] Chamberlin is not quite so precise on how oligopolists will react to price increases, but he implies that, through a series of moves, they will settle on a uniform price that will maximize the profits of each.[15] And he concludes that "the equilibrium result is the same as though there were a monopolistic agreement between them."[16]

[9] Mund, *The Application of Economic Analysis to Antitrust Law Policy*, PROCEEDINGS TWENTIETH ANNUAL CONFERENCE OF THE PACIFIC COAST ECONOMIC ASS'N 80 (1942).

[10] MACHLUP, THE BASING-POINT SYSTEM 250-251 (1949); Fetter, *Exit Basing Point Pricing*, 38 AM. ECON. REV. 815-827 (1948).

[11] EDWARD CHAMBERLIN, THE THEORY OF MONOPOLISTIC COMPETITION, esp. c. 3 (1932).

[12] ARTHUR ROBERT BURNS, THE DECLINE OF COMPETITION 40 *ff.*, 526, esp. 529, 589-590 (1936).

[13] See, for example, Brief of Respondents-Petitioners, Vol. I, Appendix A, Aetna Portland Cement Co. v. Federal Trade Comm'n, 157 F. 2d 533 (C. C. A. 7th 1946); Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948) *passim*, and United States v. American Tobacco Co., 328 U. S. 781 (1946).

[14] As Chamberlin puts it: "Since the result of a cut by anyone is inevitably to decrease his own profits, no one will cut. . . ." CHAMBERLIN, *op. cit. supra* note 11, at 48.

[15] He says: "When a move by one seller evidently forces the other to make a counter-move, he is very stupidly refusing to look further than his nose if he proceeds on the assumption that it will not." *Id.* at 46.

[16] *Id.* at 48. Chamberlin recognizes that uncertainty as to how any seller will react may force prices below the monopoly level. Paul Sweezy has argued that oligopolists will follow price cuts, but may not follow price advances. This creates a "kink" in the demand curve confronting an oligopolist and makes for stable prices somewhat below the monopoly level. See Sweezy, *Demand Under Conditions of Oligopoly*, 47 J. POL. ECON. 568 (1939).

This is the theoretical basis for the doctrine that basing-point pricing is a spontaneous evolution. Clark was among the first to expound basing point pricing in terms of oligopoly.[17] He regards basing point pricing as a form of imperfect competition that arises in industries in which some form of imperfect competition is inevitable. Industries using it have four characteristics or "predisposing conditions." (1) They produce a standardized product; (2) they produce from isolated plants or clusters of plants scattered throughout the country, each plant or group of plants having a local market within which the local firms have a comparative freight advantage (a monopoly of location); (3) freight charges on the product are high in relation to value; but not high enough to dissuade sellers from reaching out for additional business, even if to do so they must accept a lower mill price (that is, absorb freight) on the additional business; and (4) operating costs per unit of output are constant over a wide range of output up to the absolute limits of capacity—that is to say, short term marginal costs are constant and consistently below total unit cost. For cement, of which Clark made a detailed study as consultant to defendants in the Federal Trade Commission proceedings, marginal costs are about half of total average costs—long run supply price including a moderate return on investment. Other characteristics of industries in which basing point pricing has become a matter of public policy—characteristics that Clark does not specifically enumerate but neither does he ignore—include (1) a large fixed investment in specialized plant and equipment; (2) below capacity operation over long periods; (3) an inelastic demand at prices for an output less than that of the industry's capacity; and (4) only a few sellers within any particular market.

These are the characteristics which lead firms to price on what Clark calls the "oligopoly principle."[18] A seller of a standardized product knows that he can get no more for his product than any other seller, and that if he reduces his prices his rivals will cut theirs. Thus he may gain little or no business from his rivals by cutting prices. Where demand is inelastic, price cutting is doubly unattractive because not only will all rivals meet the cut, but also increased sales will bring lower gross revenue to all sellers. At the lower price each will do a lower dollar volume of business. Where marginal costs are well below total unit cost, competition which reduced prices to marginal costs would mean bankruptcy.[19] With capital facilities fixed and specialized, below-cost selling might continue for a long time without establishing equilibrium in the industry. Hence sellers who take account of the total influence of their decisions on the market will not try to get business by reducing prices. Nevertheless, in times of slack demand they are under great pressure to increase sales. They try to do so not by cutting prices on all

[17] Clark, *Basing Point Methods of Price Quoting*, 4 CAN. J. ECON. AND POL. SCI. 477 (1938).

[18] Clark, *Imperfect Competition Theory and Basing-Point Problems*, 33 AM. ECON. REV. 283, 288 *ff*. (1943).

[19] *Ibid.* Clark says: "If they did go to marginal cost, the industry in general would go bankrupt, being unable to cover operating expenses, let alone any return on investment." I believe this statement is inaccurate, or if accurate, unclear. I should think that a firm's marginal costs, if constant throughout the range of normal operating rates, would be its per unit operating expenses.

sales, but by matching the delivered prices of their rivals in areas where they are at a freight disadvantage. To overcome this freight disadvantage, they absorb freight and take a lower mill-net price. It pays to reach out for business as long as the difference between the delivered price and the freight charge exceeds marginal cost. Any price above marginal cost helps to meet overhead expenses. Self-interest will lead a seller to accept the base price of his rival when selling in territory freight-wise nearer to his rival than to his own mill.[20]

II

How the Schools Differ

The two schools, as represented by Clark and Mund, obviously differ in two respects. Mund believes that businessmen conspire to use the basing point system to obtain monopoly prices. Clark believes that, acting independently, businessmen adopt the basing point system to avoid ruinous competition. He argues that while the basing point system tends to prevent prices from falling to strictly competitive levels—marginal costs—it does not insure monopoly earnings.[21] Either "chiseling" or self-restraint will lead to prices that in the long run yield only a reasonable return on investment.[22]

Despite the clash between them, neither Clark nor Mund is wholly wrong. Clark is on solid ground in contending that basing point prices are generally below a monopoly level and in recognizing the usefulness of the theory of oligopoly as an analytical tool. Mund is on solid ground in contending that basing point pricing has generally been a part of a broader program of concerted action to restrain competition. Clark, concerned primarily with developing a theoretical explanation

[20] Why fear of invasion of his "natural" market area by his rivals, who will resort to counter freight absorption sales with ultimate reduction in earnings for everyone, will not deter any seller from initiating such invasions is not entirely clear. If demand were distributed equally over the total market for the product and if plants were equidistant and of optimum size, the theoretical solution would be one of local monopoly with neither price cutting nor freight absorption. Clark, however, states: "The possibility that an extension of A's freight-absorbing sales in B's territory will provoke an equal extension of freight-absorbing sales by B in A's territory is far less traceable or certain; and sellers are not in fact much deterred by this prospect. Each knows that, if he stopped absorbing freight, that would have little or no effect in causing others to stop making freight-absorbing sales in his area, unless demand were pressing against productive capacity." *Id.* at 290. This is the reverse of Clark's reasoning in explaining why sellers will not openly cut prices. If, as Stigler avers, basing point pricing results primarily from geographic instability in demand and involves an ebb and flow of sales in response to shifting centers of demand, with little or no cross-hauling, the inconsistency disappears. Stigler, *A Theory of Uniform Delivered Prices*, 39 AM. ECON. REV. 1143 (1949). The implications of Stigler's theory to the contrary notwithstanding, cross-hauling with freight absorption has been a continuous phenomenon in steel and cement at any rate—with a tendency to diminish in boom times and increase in depression.

[21] See Clark, *The Law and Economics of Basing Points: Appraisal and Proposals*, 39 AM. ECON. REV. 430, 440-441 (1949).

[22] Clark, *Basing Point Methods of Price Quoting*, 4 CAN. J. ECON. AND POL. SCI. 477, 481-482 (1938): "The actual base price policy of producers appears to be a form of compromise . . . which, under reasonably normal conditions of demand, may be expected to yield what they conceive as a fair return." This does not mean of course that prices are at the socially desirable level.

of basing point pricing, has ignored the arrangements that have helped to keep prices above a competitive level (*i.e.*, above marginal costs).[23]

A. The Cement Case

The Federal Trade Commission found that cement manufacturers had conspired to use the basing point system and the Supreme Court has upheld the finding.[24] For purposes of economic analysis, however, the facts—which the evolutionary school have ignored—may be more important than the law. Space permits only a summary of the facts. They are fragmentary but not meaningless. They disclose a long and persistent record of concerted action among cement producers to limit competition. The general attitude of producers is reflected in the oft-quoted statement by John Treanor, formerly president of the Riverside Cement Company and trustee of the Cement Institute:[25]

[23] Clark would be on sounder ground if he argued that in industries of the sort about which he is theorizing, businessmen will collaborate to prevent competition from injuring them, and that collaboration may eventually develop a set of practices and a code of ethics to which they will continue to subscribe long after their initial understanding. This would bring Clark pretty close to Mund.

Only in Clark's two most recent discussions does he recognize that concerted action has anything to do with basing point pricing. See *The Law and Economics of Basing Points: Appraisal and Proposals*, 39 AM. ECON. REV. 430 (1949), and *Machlup On the Basing-Point System*, 63 Q. J. ECON. 315, esp. 317 (1949).

Clark now implies, without specifically saying so, that conspiracy may play a considerable role. But he implies also that the *making of prices* (that is, the actual setting of base prices) as distinct from the *method of pricing* merely reflects independent decisions by oligopolists. According to this view, oligopolists determine base prices after taking account of the indirect as well as the direct effects of their decisions. If this is correct, it means that conspiracy on pricing methods makes it possible for oligopolists to exert the influence on prices that according to Chamberlin they will exert if they behave rationally; that is, conspiracy enables them to act according to the oligopoly principle. See *The Law and Economics of Basing Points*, *supra*, esp. 439.

Corwin Edwards, an able exponent of basing point theory and practice, falls between the two schools. See his *Basing Point Decisions and Business Practices*, 38 AM. ECON. REV. 828-842 (1948); *Doing Business Under the Present Law About Delivered Prices*, speech before the Philadelphia Chamber of Commerce, January 25, 1949; *Trends in the Enforcement of the Antimonopoly Laws*, speech before the American Business Law Institute, New York City, December 28, 1949; *The Effect of Concentration of Economic Power*, speech before the Institute of Economics and Finance, Occidental College, Los Angeles, January 28, 1950. He recognizes that conspiracy frequently accompanies basing point pricing but he rejects mandatory f.o.b. pricing as a remedy, and he makes some nice distinctions that neither the Mund-Fetter nor Clark group makes. Apart from problems of price discrimination, as to which he does not think the basing point system raises problems different from those raised elsewhere, he regards the main issue as whether or not basing point pricing results only from conspiracy or whether it may originate in independent action. He thinks that rigorous competition, independent oligopolistic pricing, and conspiracy might all lead to identical delivered pricing at any point (but he thinks markets are so imperfect that price identities under competition are likely to be recurrent rather than continuous). But he thinks that price behavior will differ under the three circumstances. Under competition any rival may initiate a change and price changes are likely to occur frequently. Under non-collusive oligopoly any seller may initiate a price change—for fear a rival will if he doesn't, even though he knows his rival will follow—but price changes will be made more reluctantly and less frequently than under competition. Under a conspiratorial basing point system—the essence of which is an allocation of the right to take the lead in price changes—the same mills will always initiate changes and, because they know others will never lead but will always follow, prices are apt to be higher and more stable than under either competition or non-collusive oligopolistic pricing.

[24] Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948).

[25] Letter of May 17, 1934, from John Treanor to B. H. Rader, Chairman of the Code Authority for the Cement Industry, Respondent's Brief, p. 127, Aetna Portland Cement Co. v. Federal Trade Comm'n, 157 F. 2d 533 (C. C. A. 7th 1946).

Do you think any of the arguments for the basing-point system which we have thus far advanced will arouse anything but derision in and out of government? I have read them all recently. Some of them are very clever and ingenious. They amount to this however: that we price that way in order to discourage monopolistic practices and to preserve free competition, etc. This is sheer bunk and hypocrisy. The truth is of course —and there can be no serious, respectable discussion of our case unless this is acknowledged—that ours is an industry above all others that cannot stand free competition, that must systematically restrain competition or be ruined.

Mr. Treanor recognized that the systematic restraint of competition required concerted action. He denied the "spontaneous evolutionary" doctrine in stating that cooperation cannot always "be left to the mutual spontaneous adoption of considerate policies on the part of each and every competitor. . . . The practical need for argument, persuasion, conferences, exchange of assurances, soon appears." He laments that by "gradual steps even the most righteous upholder of the laws, finding himself in a competitive industry, may also find himself drawn into the realm of law evasion, or even of downright law violation in the form of deliberate price fixing."[26]

Concerted action to restrict competition in the cement industry began early in this century and continued, though with interruptions, at least until the Federal Trade Commission instituted its proceedings in July, 1937. Concerted action, although not always formal, expressed itself through the following organizations or instruments: (1) Association of American Portland Cement Manufacturers, 1902-1916; (2) Association of Licensed Cement Manufacturers, 1907-1911; (3) Portland Cement Association, 1916-1919; (4) Cement Manufacturers Protective Association, 1916-1922; (5) Cement Institute, 1929-1937; (6) N.R.A. Code Authority, 1933-1935; (7) "Compendium of Established Terms and Marketing Methods," 1935-1937.[27]

Some of these agencies operated only in particular geographic areas; others operated nationally; some were encouraged or even authorized by the government; others ran afoul of the law; some operated a short time, others a long time. But whether national or regional, legal or illegal, long- or short-lived, each and all at one time or another sponsored joint action to restrict competition in the sale of cement. They led to understandings—specific or tacit—covering basing point pricing; the use of freight books showing freight rates or "common freight factors" from production centers to all delivery points; restrictions in the use of trucks for delivering cement; standardization of cement; diversion of shipments; standardization of trade practices; and the exchange of trade statistics.[28] These understand-

[26] Brief in Support of Complaint, Vol. II, p. 261, The Cement Institute, Docket No. 3167, 37 F. T. C. 87 (1943).

[27] The dates indicate either the life span of the organization or the period during which producers cooperated to limit competition. I have arbitrarily assumed that concerted action stopped when the Federal Trade Commission instituted proceedings against the Cement Institute in July, 1937. Actually the Institute was still in existence when the circuit court handed down its decision in Aetna Portland Cement Co. v. Federal Trade Comm'n, 157 F. 2d 533 (C. C. A. 7th 1946).

[28] See The Cement Institute, 37 F. T. C. 87, 143-161 (1943); United States v. Cement Mfrs' Protective Ass'n, 294 Fed. 390 (S. D. N. Y. 1923), *generally*, and see for *freight factors:* The Cement Insti-

ings facilitated if they did not insure the quotation of identical prices by all sellers of cement at any point of delivery. They also contributed to an *esprit de corps*, a code of ethics, which made the non-conformist a "chiseler," held in about the same esteem by his associates as a labor "scab" by the union. They tended to convert basing point pricing from a method of quoting prices into a system for stabilizing them. They apparently offer a more adequate explanation of the initiation and operation of basing point pricing in cement than economic theory alone has provided.

B. Collaboration in Steel Pricing

The record of concerted action in the steel industry is as notorious as that of cement, although perhaps less well authenticated. But whatever its legal status, concerted action has helped greatly to insure the use of basing point pricing as a device for restricting competition in the sale of steel. As with cement, so with steel, the record of concerted action in pricing dates back a half-century. It includes pooling arrangements; trade meetings; the famous Gary dinners; Pittsburgh Plus;[29] an N.R.A. Code of Fair Competition administered by the American Iron and Steel Institute, providing specifically for basing point pricing, designating the basing points, and fining those who violated the Code's provisions;[30] collaboration in establishing base prices;[31] compilation of freight-rate books showing freight from production centers to delivery points;[32] prescription of arbitrary rates because of the

tute, *supra*, at 143, 162 *ff*., United States v. Cement Mfrs' Protective Ass'n, *supra*; *trucking:* Petitioner's Brief, Appendix A, Vol. III, pp. 1401-1694, 1834, 1851-1860, 2112, Aetna Portland Cement Co. v. Federal Trade Comm'n, 157 F. 2d 533 (C. C. A. 7th 1946), Commission's Brief, pp. 130-161, Aetna Portland Cement Co. v. Federal Trade Comm'n, *supra*, The Cement Institute, *supra*, at 191-195; *diversion:* The Cement Institute, *supra*, at 199; *exchange of trade statistics:* United States v. Cement Mfrs' Protective Ass'n, *supra*, at 391; Petitioner's Brief, Appendix A, Vol. I, pp. 557 *ff*.; Aetna Portland Cement Co. v. Federal Trade Comm'n, *supra*, *id*., Vol. IV, pp. 2560, 2597-2598; *identical prices basing-point system:* Petitioner's Brief, Appendix A, Vol. I, pp. 135-136, Aetna Portland Cement Co. v. Federal Trade Comm'n, *supra*; United States v. Cement Mfrs' Protective Ass'n, *supra*, at 395.

[29] See United States v. United States Steel Corporation, 251 U. S. 417 (1920). Concerning Pittsburgh Plus, Judge Gary stated:

"It was deemed necessary for the orderly conduct of the business to have *one basing price* . . . so that every user of steel all over the country bought and used his steel on a certain basis, knowing in advance that everyone else who bought steel had to pay exactly as he did, *with the addition of the increased freight depending upon where he wanted to use the steel.*" United States Steel Corporation, 8 F. T. C. 1, 33 (1924).

[30] I NRA, CODES OF FAIR COMPETITION, *passim*, esp. 189, 198 (1933). *Cf*. also FTC, REPORT TO THE PRESIDENT IN RESPONSE TO EXECUTIVE ORDER OF MAY 30, 1934, WITH RESPECT TO THE BASING POINT SYSTEM IN THE STEEL INDUSTRY (1935); FTC, REPORT ON THE STEEL CODE TO THE PRESIDENT OF THE SENATE PURSUANT TO SENATE RESOLUTION No. 166 5-8 (1934).

[31] FTC, REPORT TO THE PRESIDENT, *op. cit. supra*, note 30; FTC, REPORT ON THE STEEL CODE, *op. cit. supra*, note 30.

[32] Benjamin F. Fairless, Chairman of the Board, United States Steel Corporation, testified before the TNEC that:

"The American Iron and Steel Institute has a traffic committee composed of traffic managers of 10 different steel companies. This committee supervises the institute's Freight Rate Book . . . and the responsibility of keeping these sections up to date is assigned to different members of the committee. When corrections are necessary—and by necessary I mean when rate changes take place—these committee members have the changes made on supplementary sections or pages, sending these sections or pages to the institute for distribution to holders of the rate book." *Hearings before the TNEC*, pt. 27, 76th Cong., 3d Sess. 14222-14223 (1940).

See also letter presented in Commission's Brief, pp. 171-172, quoted in FRITZ MACHLUP, THE BASING-POINT SYSTEM 128 n. (1949).

diversity of switching charges;[33] collaboration in determining the price of "extras";[34] and ratification of a resolution on the death of NIRA to maintain the standards of fair competition as set forth in the Code.[35]

As with cement, so with steel, the government at times has encouraged, even required, concerted action to limit competition. As with cement, so with steel, collaborative action has been an educational process designed to insure uniform and predictable behavior by rival sellers under the leadership of the United States Steel Corporation.[36] Industry members have tried to educate themselves and each other to behave as economists have argued that informed, intelligent oligopolists will behave. But education has not been enough, and when the going has gotten rough "chiselers," even when faced with formal machinery designed to prevent it, have upset a precarious equilibrium at prices above competitive levels.

C. Freight Equalization in Selling Bottle Caps

Crown bottle caps consist of cork discs enclosed in metal shells. Bottling industries use them to close bottles. Their manufacture and sale does not conform exactly to Clark's specifications of industries that fall naturally into a basing point pricing pattern, but it comes close to doing so. It *may* differ in that crown bottle caps are light and freight charges are a relatively unimportant part of delivered costs.[37] But caps are standardized and a small difference in price will shift business from one supplier to another. Demand for bottle caps is derived from the demand for the bottled beverages whose containers they cap and is therefore highly inelastic. The price of the cap is such a small part of the price of the bottled beverage that a large percentage drop in the price of caps would probably bring no increase in their use. Their production is highly mechanized, and operation below plant capacity probably results in constant marginal costs substantially below total unit costs throughout the normal range of operations. Price competition during periods of slack demand, therefore, is apt to be "ruinous," *i.e.*, it is likely to drive prices

[33] Exhibit No. 2206, *Hearings before the TNEC*, pt. 27, 76th Cong., 3d Sess. 14435 (1940). Also, Wooden and White, *An Analysis of the Basing Point System of Delivered Prices as Presented by the United States Steel Corporation in Exhibits Nos. 1410 and 1418*, in THE BASING POINT PROBLEM 94 (TNEC Monograph 42, 1941).

[34] Cf. testimony of Benjamin F. Fairless, in *Hearings before the TNEC*, pt. 19, 76th Cong., 2d Sess. 10560 (1940).

[35] Mr. James Brackett of the United States Steel Corporation wrote the Executive Secretary of the Temporary National Economic Committee on December 18, 1939, that so far as he knew the 1935 policy had not been modified. See *Hearings before the TNEC*, pt. 27, 76th Cong., 3d Sess. 14232 *ff.* (1940); see also, Wooden and White, *supra* note 33.

[36] Eugene G. Grace, President of the Bethlehem Steel Co., and of the Bethlehem Steel Corporation, on November 9, 1939 testified before the Temporary National Economic Committee that ". . . one of the principal factors which we have in that process of reaching decisions as to what we will do sales-wise as a rule has been the announcement of the Steel Corporation from time to time periodically as to what their prices are to be." *Hearings before the TNEC*, pt. 19, 76th Cong., 2d Sess. 10586 (1940). He also stated that during the 1938 depression, when competition had forced actual steel prices below quoted prices, he ". . . was very glad . . . of the opportunity to follow the Corporation's lead in the publishing of new base prices, which they did. I was glad to see that take place. I thought then it was constructive and a good thing to do." *Id.* at 10592.

[37] This is a question of fact about which I am not sure. Data are not available to answer it.

well below total unit costs. And finally, a few sellers dominate the business. Crown Cork & Seal has about 50 per cent of the market. With six others, it controls 85 per cent.

Here then is an industry where the likelihood of pricing in accordance with the "oligopoly principle" is great. On purely theoretical grounds producers might be expected to refrain from active price competition without resorting to conspiracy. Moreover conspiracy is easy to conceal, and an order forbidding it hard to enforce.

How in fact have manufacturers priced bottle caps? Have they conspired in doing so? Both the Commission and the circuit court have answered these questions.[38] They found that since 1921 manufacturers have quoted prices for bottle caps f.o.b. their plants. All have equalized delivered prices at any delivery point at any time, absorbing freight when necessary to do so. Although sometimes referred to as "universal freight equalization," this method of selling works like basing point pricing with every production center a basing point. From 1938 to 1948 all producers sold bottle caps at identical and unchanging prices.[39] All sellers also used identical schedules of discounts, additions, and differentials. Since all buyers at any delivery point were always quoted the same delivered price regardless of from whom they bought, they apparently could not influence prices by turning from one seller to another. Without proof of any express agreement to charge uniform base prices, the Commission found "that the respondents have in fact entered into . . . and carried out an understanding, agreement, combination or conspiracy . . . to restrain and suppress competition in the sale of their products."[40] What was the circumstantial evidence to support the finding? In 1925 the leading manufacturers of bottle caps organized themselves into a trade association. Shortly thereafter, through the efforts of the association, all members standardized their bottle caps even to colored decorations. At an early meeting of the association, members discussed ways of insuring that all would charge the same delivered price for their standardized product. They decided that the best way to do this was to incorporate a schedule of deductions, additions, and differentials into a standard form of contract. The members, however, never formally adopted a standard contract. In truth, they have since used no contract form but have quoted prices informally by correspondence or through oral negotiation. In 1933, Crown Cork & Seal licensed most other manufacturers to use its patents and the licensees agreed not to sell caps for less than Crown Cork & Seal did. To aid them in complying with the arrangement, Crown Cork & Seal supplied each licensee with its price list. Moreover, it adjusted a patent lawsuit with one of its rivals by an exchange of licenses and, although neither litigant used the other's patents, each thereafter exchanged price lists. Crown Cork & Seal continued to furnish its rivals with its price list until shortly before the Commission began its proceedings against the

[38] Bond Crown & Cork Co. v. Federal Trade Comm'n, 176 F. 2d 974 (C. C. A. 4th 1949).

[39] Before this period price changes were infrequent, and with minor variations all sellers charged the same price.

[40] Bond Crown & Cork Co. v. Federal Trade Comm'n, 176 F. 2d 974, 977 (C. C. A. 4th 1949).

industry in 1941. As previously stated, all sellers for more than a decade charged precisely the same delivered price to any designated point.

The Commission concluded from all these circumstances that "an understanding or agreement under which the respondents acted and still act in concert may be inferred."[41] In supporting the Commission's findings the circuit court, quoting from *Fort Howard Paper Co. v. Federal Trade Commission*,[42] said: "The essential combination or conspiracy may be found in a course of dealings or other circumstances as well as in any exchange of words."

In view of all the circumstances of this case, a wayfaring economist, making an excursion into a legal maze, may perhaps be justified in concluding that the Commission's and the court's findings make sense.

In other industries using basing point pricing, against which the Commission has proceeded, the evidence of conspiracy has been even more specific and more convincing.[43]

D. The Glucose Cases

In only two cases where the Commission has condemned basing-point pricing has conspiracy not been charged and proven. These are the so-called glucose cases. In these cases the Commission proceeded under the price-discrimination prohibitions of the Robinson-Patman Act. The essential facts in the *Corn Products Refining Company* case follow.[44] The Corn Products Refining Company made glucose in two plants—one at Chicago, the other in Kansas City. It quoted prices for any delivery point, whether the sale was from Chicago or Kansas City, at the Chicago base price plus rail freight from Chicago. As a result, on sales to buyers from its Kansas City plant, when located freightwise nearer Kansas City than to Chicago, the company charged a so-called "phantom-freight." On sales from its Kansas City plant to buyers freightwise nearer Chicago than Kansas City it absorbed freight. Thus its mill-nets (corresponding to an f.o.b. price at Kansas City) varied with the location of the buyers. Buyers close to the Kansas City plant frequently paid more for glucose than more remote buyers. The Commission found that such price discrimination injured competition among candy manufacturers, some of whom had been forced to relocate at or near Chicago in order to survive. The Commission held that such price discrimination violated the Robinson-Patman Act and forbade it. A similar principle was involved in the *Staley* case.[45] In both cases,

[41] *Id.* at 976.

[42] 156 F. 2d 899, 905 (C. C. A. 7th 1946).

[43] United States Steel Corporation, 8 F. T. C. 1 (1924); Corn Products Refining Co. v. Federal Trade Comm'n, 324 U. S. 726 (1945); Federal Trade Comm'n v. A. E. Staley Mfg. Co., 324 U. S. 746 (1945); Federal Trade Comm'n v. The Cement Institute, 333 U. S. 683 (1948); Triangle Conduit and Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *aff'd per curiam sub nom.* Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949); United States Maltsters Ass'n v. Federal Trade Comm'n, 152 F. 2d 161 (C. C. A. 7th 1945); Fort Howard Paper Co. v. Federal Trade Comm'n, 156 F. 2d 899 (C. C. A. 7th 1946); Milk and Ice Cream Can Institute v. Federal Trade Comm'n, 152 F. 2d 478 (C. C. A. 7th 1946).

[44] Corn Products Refining Co. v. Federal Trade Comm'n, 324 U. S. 726 (1945).

[45] Federal Trade Comm'n v. A. E. Staley Mfg. Co., 324 U. S. 746 (1945).

basing point pricing injured competition among the buyers of glucose. While these cases did not involve a charge of conspiracy, the history of the glucose industry reveals a long record of concerted action to eliminate price competition[46] and, had it chosen, the Commission might have proceeded in the glucose cases under Section 5 of the Federal Trade Commission Act.

Certainly such facts as are available regarding concerted action by business rivals using basing-point pricing lends little support to the doctrine of spontaneous evolution. Even where sellers are few, and a rational consideration for the total consequences of their decisions would be expected to lead to pricing on the "oligopoly principle" without any collusion, they have in fact found concerted action essential to restrain price competition.

III

Economic Consequences of Basing Point Pricing

The economic consequences of basing-point pricing are as important to sound public policy toward it as are the factors that have brought it about. The acceptability of any "competitive" arrangement depends on whether or not other arrangements would work better. There are three practical alternatives: (1) mandatory f.o.b. pricing; (2) basing point pricing maintained through concerted action—overt or tacit; and (3) non-conspiratorial pricing with sellers free to sell as they wish, even to absorbing freight, subject only to rules laid down by Congress designed to preserve competition.

For three reasons this study rejects mandatory f.o.b. pricing. In the first place, as long as the organization and control of those industries practicing basing point pricing is undisturbed, and as long as industries are as free as they have been to act concertedly rather than independently on prices and production policies, mandatory f.o.b. pricing will not necessarily make competition more effective than it has been in basing point industries. Businessmen can agree on marketing areas as well as on pricing policies. Unless restrained from doing so, they might work out understandings, more or less tacit, about where each will sell and at what prices. Price leadership might be as effective under f.o.b. pricing as under basing point pricing. Oligopolistic behavior (that is the tendency for rivals to take account of the indirect as well as the direct consequences of their decisions) can be supple-

[46] See Myron Watkins, Industrial Combinations and Public Policy, c. X (1927); FTC, Corn Products Refining Co., Docket No. 5502, Complaint, June 20, 1947; Docket No. 927, November, 1922; United States v. Corn Derivatives Institute, consent decree, 1932; Complaint, Docket No. 3633, October, 1938; Complaints, Docket Nos. 3798, 3799, 3800, 3801, 3802, 3803, 3804, 3805, June, 1939; Cease and Desist Order, Docket No. 3798, September 26, 1940; also Cease and Desist Orders Nos. 3802, Nov. 2, 1940, 3804, December 11, 1940, 3805, March 15, 1941, 3801, April 3, 1941, 3800, March 17, 1942, and 3803, June 10, 1942. For the court rulings, see Corn Products Refining Co. v. Federal Trade Comm'n, 144 F. 2d 211 (C. C. A. 7th 1944); A. E. Staley Mfg. Co. v. Federal Trade Comm'n, 144 F. 2d 221 (C. C. A. 7th 1944); Corn Products Refining Co. v. Federal Trade Comm'n, 324 U. S. 726 (1945); Federal Trade Comm'n v. A. E. Staley Mfg. Co., 324 U. S. 746 (1945). Also see Motion to Dismiss Complaint, Corn Products Refining Co., before the Federal Trade Comm'n, Docket No. 5502, September, 1948.

mented by concerted action to curb competition under either mandatory f.o.b. selling or basing point pricing.[47] In the second place, if mandatory f.o.b. pricing should not be accompanied by tacit agreements, marketing areas, and the like, it might seriously disturb the pattern of plant location that has developed under basing point pricing, encouraging plant expansion in new areas and forcing sharp devaluation of plant and equipment in areas of surplus capacity. In the long run this would be economical, but its immediate effects might be disturbing, particularly if and when business activity generally declines.[48] In the third place, to tell businessmen that they must price their products f.o.b. when in their individual judgment freight absorption might prevent bankruptcy or enhance their profits, seems inconsistent with the function of the *entrepreneur* in a competitive society. Positive state interference of this sort is apt to lead to the government's assuming further responsibility in the guidance of individual enterprise. Eventually the government may so encroach on individual liberty in business matters that it has no alternative but to take over industry.

Let us consider then alternatives (2) and (3). Non-conspiratorial pricing with individual firms free to sell with the right to absorb freight if they want to as long as they do not violate rules laid down by Congress to preserve competition, apparently has two advantages over conspiratorial basing point pricing. (1) Except at the height of a business boom when capacity is fully utilized, it would make for lower prices and it would probably make for more flexible prices at all times. (2) It would tend to insure a more economical use of resources.

A. Basing Point System Makes for Higher Prices

A characteristic of the major industries which have relied on basing point pricing along with a lot of complementary paraphernalia to restrain competition is that they have operated below full capacity over long periods. This is true of the cement and steel industries, both of which operated well below capacity throughout the period between the two world wars. The object of concerted action has been to keep cost-price margins high—that is, higher than they would have been in the

[47] There is an important distinction between the above argument and that of Clark. See Clark, *Basing Point Methods of Price Quoting*, 4 CAN. J. ECON. AND POL. SCI. 477 (1938). Clark thinks that if businessmen are required to sell f.o.b. they may for a brief period engage in ruinous competition, after which they will discover some other arrangement that will more adequately protect their interest. The above argument does not imply that businessmen should not be prevented from conspiring in one way merely because they *might* find some other way to conspire. The problem is to find a way to prevent conspiracy, not a way to enforce f.o.b. selling.

If Stigler is correct in his theory that geographic fluctuation in demand is the main force behind basing point pricing arrangements, it would be difficult for rivals to work out acceptable agreements on market areas. I think it would be difficult even though I do not accept fully Stigler's theory, but I do not think it would be impossible.

[48] The argument that mandatory f.o.b. pricing should not be required merely because it may correct a pattern of location which has arisen as a result of arbitrary pricing of another sort is not of itself compelling. But the third alternative offers a better way of doing the same job. There are other reasons for rejecting mandatory f.o.b. pricing. See Kaysen, *Basing Point Pricing and Public Policy*, 63 Q. J. ECON. 289 (1949), who develops a convincing argument that f.o.b. pricing is unlikely to make prices more flexible or lower than basing point pricing.

absence of concerted action. To do this, both industries formulated specific trade practices and encouraged self-discipline through a code of business ethics designed to reinforce the "natural" tendency of an oligopolist to take account of his rivals' probable reactions in formulating his own business policies. While this did not always prevent "chiseling" and at times not even an erosion of the price structure, the very fact that business leaders persisted in it over long periods indicates that it paid off. Businessmen do not surrender their individual discretion on pricing and production policies for the fun of it. They have tried to advance their individual interests by promoting the interest of their group.

In oligopolistic markets any seller, of course, may be reluctant to cut prices because he fears that his rivals will promptly meet the cut. When sellers are acting independently, this fear may not prevent some producer, because of the urgency of his needs or the temporary advantage he hopes to gain, from initiating a price cut which others may be forced to follow.

But oligopolists acting independently may be equally reluctant to raise prices, except in periods of capacity operation, for fear their rivals will not follow. The basing point system removes this fear. Where faithfully followed, basing point pricing enables any base mill to raise prices with the knowledge that other mills will not sell for less in the area where its base price governs. At most the price increase will have broadened the area within which other base prices govern and the area within which the other mills can profitably absorb freight. If other base mills follow the price increase, the initiator need suffer no loss of business to rivals. In technical language, basing point pricing may be a means of eliminating the "kink" in the demand curve facing an oligopolist.[49]

This helps to explain why cement producers raised base prices of cement in the second half of 1932 and the first half of 1933 despite a drastic decline in demand. That the steel industry's pricing methods have kept steel prices abnormally high is suggested by the slight response that changes in the percentage of capacity at which the industry has operated have brought in the price of steel. With the industry operating at 98 per cent of its steel ingot capacity in 1942, average delivered prices actually paid for hot rolled sheets were 101 per cent of published delivered prices; for cold sheets, 101 per cent; for hot rolled strips, 100 per cent; for plates, 102 per cent; and for structural shapes, 101 per cent. Three years earlier, in the second quarter of 1939, with the industry operating at only 51 per cent of its steel ingot capacity, and published prices substantially the same, on the average an 8 per cent concession from published delivered prices was made for hot rolled sheets; a 5 per cent concession for cold rolled sheets; an 8 per cent concession for hot rolled strips; and only a 3 per cent concession each for plates and for structural shapes.[50]

[49] See Sweezy, *Demand Under Conditions of Oligopoly*, 47 J. POL. ECON. 568 (1939).

[50] Fazar and Bean, *Labor Department Examines Consumers' Prices of Steel Products*, 157 IRON AGE 118-145 (April 25, 1946); and Kaysen, *supra* note 48, at 298.

Steel prices were so high in 1938, a year of depression, that the Steel Corporation could break even while operating at from 40-45 per cent of capacity.[51]

B. Basing Point System Makes for Higher Costs

But not only does systematic and concerted basing point pricing make for higher margins than would prevail without it, it also tends to keep costs high. Two factors contribute to this. In the first place, when price competition is eliminated in the sale of a standardized product, business rivals must rely largely on sales effort to obtain business. Since salesmen may perform other functions besides trying to get orders—as for example, the actual taking of orders, giving advice on specifications and on the adaptability of a product for a particular use, etc.—not all expense for salesmen represents an added cost. However, when the new manager of the Bay City, Michigan plant of the Aetna Portland Cement Company abandoned price cutting in 1936, following a protest from its trade rivals to the president of Aetna and the firing of its old manager, and began to sell "according to the ethics of the industry," he had to increase his sales force "in the process of getting business on a new basis."[52]

Even oligopolists who are free to sell as they see fit, if they quit acting in concert and make their own decisions, are likely to be forced to rely more on price than on sales effort to get business. At times, however, they no doubt will reach out for business by absorbing freight in preference to cutting their f.o.b. price which would ordinarily govern the bulk of their sales. When they do, they may prefer to meet their rivals' delivered price rather than to cut below it. They are therefore likely to use some salesmen to get business, but getting sales through freight absorption is a game two can play. Since freight absorption means lowered mill nets, if they do not conspire to prevent it, rival sellers are likely to be driven, whether they like it or not, to rely more on price to get business than they would under concerted basing point pricing. It seems reasonable to conclude that non-conspiratorial pricing will reduce selling costs somewhat.

But increased reliance on price to get business will tend to lower costs in another way. Business firms will be forced to cut costs or go into bankruptcy. Basing point pricing through concerted action permits high cost producers to live and weakens the incentive of both high and low-cost producers to reduce costs. A price leader committed to the philosophy of live-and-let-live is apt to be more concerned with keeping his investments intact through price controls and his followers in line than in placing himself in a position to bankrupt them by cutting prices. Expenditures for group activities—compilation of freight rate books, joint determination of the costs of "extras in steel," joint advertising to increase the use of the

[51] See UNITED STATES STEEL CORPORATION, TNEC PAPERS, Vol. II, Chart Studies, p. 57 (1940). After mid-1938 price reductions, United States Steel fixed the break-even point at 50-55 per cent of capacity. See *id.* at 63.

Burns notes a report that in 1934 steel prices were such that the industry could obtain profits if they operated at 50 per cent of capacity. A. R. BURNS, THE DECLINE OF COMPETITION 543 (1936).

[52] The Cement Institute, 37 F. T. C. 87, 190-191 (1943).

product, nurturing the cooperative spirit, and the like, are apt to replace in part, at any rate, expenditures for lowering costs and improving the product.

That something like this has happened to Big Steel is suggested by its continued loss of relative position in steel production from its organization to World War II. In 1902, the United States Steel Corporation produced 65.7 per cent of the total domestic tonnage of steel ingots and castings. In 1937, it produced only 36.8 per cent. In 1902, it produced 65.4 per cent of Bessemer steel rail tonnage, 59.4 per cent of plates and sheets, and 71.5 per cent of wire rods. In 1937, it produced only 35.2 per cent of all rolled and finished products.

The Corporation's concern with protecting property values by keeping prices high has been notorious. In the words of *Fortune*:[53]

> The fact that the Corporation, simply because of the magnitude of its conception, had from the beginning so many hundreds of millions of its dollars in plant worked strongly against change. And so the chief energies of the men who guided the Corporation were directed to preventing deterioration in the investment value of the enormous properties confided to their care. To achieve this, they constantly tried to freeze the steel industry at present, or better yet, past levels.

As late as 1938, the Corporation's subsidiaries are said to have lacked a comprehensive system of modern cost accounting and to have had cost and production control methods far below the customary standards in other industries. According to *Fortune*, as of 1936 the Corporation had contributed very little to the art of steel making and the steel industry was one of the most technologically backward of our major industries.

Both costs and cost-price margins are likely to be higher in industries using a basing point system to restrict competition than they would be without concerted action. Prices therefore could scarcely yield monopoly results—*i.e.*, maximize earnings. In truth, a live-and-let-live policy may even be extended to include an industry's customers. At any rate, as previously indicated, Clark finds that in establishing base prices in cement, price leaders have tried merely to obtain a fair return on their investment.[54] According to an analysis of prices, costs, and profits jointly prepared by Price, Waterhouse & Co. and Ford Bacon & Davis and offered by respondents as evidence in proceedings before the Commission but refused by the Commission, the respondents earned on actual cost of assets an average of less than 3 per cent over the ten year period, 1928-37.[55]

C. Basing Point Pricing Has Meant An Uneconomical Use of Resources

Both the cement and steel industries had a lot of unused capacity in good years and bad throughout the period between the two wars. Unused capacity in cement

[53] Fortune, March, 1936, p. 170. According to *Fortune*, the steel industry as of 1936 was one of the most backward of our major industries.

[54] Clark, *Basing Point Methods of Price Quoting*, 4 CAN. J. ECON. AND POL. SCI. 477 (1938).

[55] See Brief for Respondents, p. 241, Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948).

ranged from 15 per cent of the total in 1924 to 77 per cent in 1933. Unused steel ingot capacity ranged from 80.5 per cent in 1932 to 35.3 per cent in 1939. The restriction on price competition that basing point pricing exerted under these circumstances tended to make for an uneconomical use of resources in two ways: (1) It has tended to keep surplus resources in the industry and to prevent their being used economically; and (2) it has tended to insure an uneconomic use of transportation facilities.

It is beyond the scope of this study to analyze the circumstances that resulted continuously in unused capacity in cement and steel during the period under review. Capacity is not a very precise term and the figures—although based on the industry's own calculations—may be somewhat misleading. Moreover, the figures are average annual figures. Demand for both cement and steel may fluctuate seasonally and geographically, and hence over-all annual figures may conceal the fact that at certain times and in certain places plants were operating very much closer to capacity than the annual figures reveal. Recognizing this fact, it nevertheless seems reasonable to conclude that these two industries suffered from a surplus of facilities or from an underuse of facilities from 1920 to 1940. In short, resources were not used economically in these industries. By restricting output through concerted action business leaders were able to shift the burden of unused capacity from the industry to the public. This is reflected in the 3 per cent earnings of the cement industry during the period 1928-37, and a return of about 3.4 per cent on net assets of the United States Steel Corporation during the period from 1920 to 1938.[56] When viewed from the interests of these industries, this moderate rate of return suggests that price leaders have exercised such discretionary controls as they possess with considerable restraint, as does the fact that steel in post-war markets has continuously sold for less through the regular channels of trade than it has in the "gray" markets.

Nevertheless, even the moderate rate of returns realized over the period between the two wars is difficult to justify on strictly economic grounds. Continuous surplus capacity in an effectively competitive economy would have tended to drive prices so far below total unit cost as to shrink capacity. That steel ingot capacity increased by about 30 per cent from 1920 to 1939 and cement capacity increased by about 74 per cent suggests strongly that discretionary controls raised prices above a socially justifiable level. In view of the difficulty of shifting such highly specialized and fixed capital as is found in cement and steel, it is quite possible that below-cost prices would not have established a long-run "competitive equilibrium" within the period under review. Possibly, also, without any concerted action, rational oligopolistic behavior would have checked a price decline above the level of marginal costs. This analysis indicates that prices in the absence of concerted action, however, would have been lower than they have in fact been. The most important consequence of lower prices in these industries throughout the 1930's would probably have been a different distribution of income, a redistribution more favorable to spending and less favorable

[56] Exhibit No. 1391, *Hearings before the TNEC*, pt. 19, 76th Cong., 2d Sess. 10717 (1940).

to saving; and, since this was a period of under-investment, more favorable to a high level of employment and a high level of national income. The redistribution, moreover, would have reflected more accurately the unobstructed evaluation of buyers of the services rendered by cement and steel producers. Lower prices throughout this period would probably have increased somewhat the use of these products and thereby increased the real income of the community.

A defense offered by some economists for the maintenance of surplus capacity in steel and cement is that a smaller capacity would have seriously embarrassed us in the emergency of World War II. As for cement, this is not true. Only since the war has the cement industry operated at capacity. The steel shortage during World War II would have been more serious had steel prices sunk so low during the interval between the wars as to have reduced capacity. It is doubtful that non-conspiratorial oligopolistic pricing would have forced such low levels, but even if it had, it is no convincing argument for leaving price-making to the joint discretionary controls of a relatively few private producers. To shape an economy for war calls for a different type of control than to shape it for peace. Few policy makers in a democracy will want to rely on private arbitrary price making to insure adequate facilities to fight a world war. Planning for total war is a public not a private matter. It is total not fragmentary planning.

D. Basing Point Pricing Has Retarded Expansion of Low-Cost Facilities

But basing point pricing as a means of restricting competition in an industry organized and controlled as is the steel industry has resulted in an uneconomical use of facilities in a more specific way. It has retarded the expansion of facilities that could most economically serve particular geographic areas, for the benefit of facilities less favorably located.[57] For example, basing point pricing in steel has enabled Chicago and Pittsburgh producers to supply continuously markets for certain steel products that could be laid down for less by the Birmingham producers. Birmingham is a low-cost producing area. It is the only important producing center which contains within the immediate area adequate supplies of the essential raw materials—iron ore, coking coal, and lime for fluxing. It can supply not only the Texas market by cheap water transportation but the Atlantic Coast and Western markets as well. Naturally it could be expected to supply not only its home markets but other nearby markets. That it has not been permitted to do "what comes naturally" is indicated by data covering all shipments of heavy structural shapes during the month of February, 1939, by mills owning 81 per cent of total domestic capacity.[58] During this month, Birmingham received from all sources included in the sample 1,623 tons of heavy structural steel shapes. Birmingham mills supplied

[57] For an excellent discussion of this aspect of the problem, see Johnson, *The Restrictive Incidence of Basing Point Pricing on Regional Development*, 37 GEO. L. J. 149 (1949); and Edwards, *Geographic Price Formulas and the Concentration of Economic Power*, *id.* at 135.

[58] These data are obtained from unpublished returns from questionnaire Form B submitted by the TNEC. For a description of this questionnaire and a statement of its coverage, see *Hearings before the TNEC*, pt. 27, 76th Cong., 3d Sess. 14133 *ff.* and 14350 (1940).

only 1,017 tons of this, or 63 per cent of the total. Far away Chicago supplied 453 tons, the more remote Pittsburgh-Johnstown area supplied 122 tons, and even most distant eastern Pennsylvania supplied 31 tons. Average freight costs on shipments by Birmingham producers to buyers in that area were 94 cents a ton; for Chicago shipments $11.62 a ton; for Pittsburgh-Johnstown, $12.81 a ton; and for eastern Pennsylvania, $15.16 a ton. Basing point pricing made deliveries profitable to remote producers but it prevented the most economical use of the best situated facilities.

Birmingham with its home markets thus invaded, sought business elsewhere. It turned to nearby Texas where again it had a substantial delivered-cost advantage over rival producers. Nevertheless, although operating well below capacity during the period under review, Birmingham supplied only 467 tons of the total Texas market of 3,788 tons during February, 1939. The Rocky Mountain area, Chicago, Pittsburgh-Johnstown, Buffalo, and St. Louis supplied the balance in that order. The delivered price was high enough to make it profitable for such remote suppliers to reach the Texas markets by absorbing substantial amounts of freight. Average actual freight charges on shipments from Birmingham were $11.04 a ton; from eastern Pennsylvania, $12.49 a ton; from the mountain states, $13.22 a ton; from St. Louis, $14.91 a ton; from Chicago, $15.54 a ton; from Pittsburgh-Johnstown, $16.43 a ton; and from Buffalo, $22.23 a ton.

There can be little doubt that basing point pricing in steel—with all its complementary price fixing paraphernalia—has retarded the expansion of iron and steel producing facilities in the low-cost Birmingham region and prevented the economical use of existing facilities.

E. Basing Point Prices Make for Uneconomical Use of Transportation Facilities

But basing point pricing has also made for an uneconomical use of transportation facilities. Apparently Stigler overstates the case in concluding that market interpenetration is practically non-existent and in holding that market penetration is primarily a result of geographical fluctuations in demand, with products flowing from areas of low demand to areas of high demand, the direction of shipments reversing with geographic changes in demand. Actually it has been a continuous characteristic of cement and steel with a tendency to increase in periods of depression and to decrease in boom times.

The basing point system is designed to insure identical delivered prices by rival producers. It encourages producers to compete for business on a service basis rather than a price basis. It is a form of price discrimination that, when systematically practiced by all sellers, does not seriously threaten the price structure. In periods of generally slack demand, rival producers prefer to get business by reducing their mill nets on a relatively small part of their total sales and by absorbing freight, than to get it by lowering their base price to all buyers. In such periods, freight absorption increases. In boom times, when producers can get business without absorbing freight, except to keep business connections they have no incentive to accept

less on remote sales than they get on nearby sales. The post-war experience indicates that when demand outruns supply, remote buyers may find it difficult to find a supplier. Remote suppliers find it more profitable to accept only non-freight absorbing business. Nearby suppliers prefer to supply their old customers.

A single example will suffice to show that market interpenetration and freight absorption have been a two-way phenomenon in normal times. The Board of Investigation and Research discovered that during one day in November, 1939, at least 245,380 pounds of tin plate started by rail from Baltimore to Chicago and that on the same day at least 42,809 pounds of tin plate started by rail from Chicago to Baltimore.[59]

Basing point pricing makes for an uneconomical use of transportation facilities in two ways. (1) It encourages needless cross-hauling by rail freight; and (2) it discourages the use of cheaper modes of transportation—water and trucks.

Under a basing point system, delivered prices are quoted on a basis of railway freight. Buyers have not generally been free in industries where basing point systems are rigidly adhered to, to buy at the plant and deliver by the cheapest method of transportation.

Business rivals, in the absence of concerted action, would no doubt permit buyers to buy f.o.b. at such prices as the sellers customarily charged and ship the product by whatever way they chose. Business rivals no doubt also would at times prefer to absorb freight to get business rather than to try to get it by reducing their base prices to all comers. In oligopolistic industries, therefore, freight absorption with price discrimination is apt to continue even without collusion among rivals, but it is apt to be on a reduced scale.

On the whole, non-collusive, discriminatory f.o.b. pricing would likely have led to lower-price margins, more flexible prices, lower costs, and more economical use of production factors during the period between the two wars than did basing point pricing through concerted action.

IV

SHOULD THE LAW BE CHANGED?

Whether or not any change in the law is required to permit freight absorption at the discretion of business firms acting independently will depend largely on the wisdom with which the Federal Trade Commission uses the administrative powers which the Congress and the courts have given it.

Despite all the furor that the Supreme Court's decision in the *Cement* and the circuit court's decision in the *Rigid Steel Conduit* cases raised, the Commission has tried to make it clear that it will not proceed against basing point pricing under Section 5 of the Federal Trade Commission Act unless there is evidence of collusion.[60] What constitutes collusion, however, may not always be clear. In all cases

[59] CHARLES E. LANDON AND WILLIAM P. MCLENDON, THE ECONOMICS OF IRON AND STEEL TRANSPORTATION 85 (1945), printed as letter from the Board of Investigation and Research transmitting A REPORT ON THE ECONOMICS OF IRON AND STEEL TRANSPORTATION, 79th Cong., 1st Sess (1945).

[60] See statement of Commissioner E. L. Davis prepared for delivery before the Senate Subcommittee

that have thus far come before the Commission under Section 5, the record has revealed unmistakable evidence of concerted action. But the courts have indicated that the pattern of pricing behavior may itself be evidence of conspiracy. The difficulty of proving overt acts of conspiracy plus the difficulty of enforcing cease and desist orders against a practice which conspirators have learned pays, no doubt accounts for the Commission's having extended the scope of its charges and its orders in the *Rigid Steel Conduit* case to cover parallel action by rivals when the effect of the action is to restrict competition.[61] Some of the Commission's staff, who accept the Mund-Fetter philosophy, are apparently convinced that parallel action by business rivals cannot be achieved without agreement and that the only way to prevent it is to write orders that in effect leave no means of compliance but f.o.b. selling.

If this analysis is sound, such a policy is unsound. In most cases to prohibit conspiracy and ban the agencies through which it has been achieved should eventually insure independent f.o.b. pricing with sellers absorbing freight at their discretion. Where sellers are so few and so well disciplined that they will continue to act as they have jointly disciplined themselves to act, the remedy lies not in mandatory f.o.b. selling but in changing the structure of the industry so that business rivals will behave like competitors. This would involve dissolution suits, and would require cooperation between the Commission and the Department of Justice. If the Federal Trade Commission, the Department of Justice, the courts, and the electorate are not prepared to support such a program, the remedy obviously lies in other directions. But it lies in other directions because society is unwilling to pay the price of obtaining effective competition, not because it is impractical to achieve it.[62]

If the aim of public policy is to insure effective competition in the production and sale of commodities, the Federal Trade Commission will have to limit its attack on basing point pricing under the Robinson-Patman Act to two sets of circumstances: (1) where it results in phantom freight (whether obvious or concealed in price differentials) and injures competition among the buyers of the product as in the *Corn Products Refining Company* case; and (2) where a multi-plant firm engages in local price discrimination by absorbing freight, the long-run effect of which is to lessen competition by putting a local rival out of business. Again, a wise application of the law to predatory price cutting requires cooperation between the Department of Justice and the Commission, for here the basic difficulty is not price discrimination, but the concentration of economic power. Again the remedy lies in changing the structure of the industry so that survival in the competitive struggle rests on economic efficiency, not on financial power.

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on Trade Policies (January 24, 1949); and Edwards, *Basing Point Decisions and Business Practices*, 38 AM. ECON. REV. 828 (1948).

[61] See, for example, Sheehy, *The Legal and Factual Content of Recent Geographic Pricing Cases*, 37 GEO. L. J. 183-200, esp. 200 (1949).

[62] This statement is based on the historical fact that oligopolists have generally achieved their position in the market by merging with rivals and on the belief that they can be separated into several production units with no loss in efficiency. Something far short of perfect competition will suffice.

DELIVERED PRICING AS CONSPIRACY AND AS DISCRIMINATION: THE LEGAL STATUS

Bueford G. Herbert*

I

Introduction

The delivered price systems here considered are not novel or recent things, but are practices which businessmen have used for approximately half a century. It is not strange that any action which threatens to jeopardize methods of pricing which have become to most businessmen settled and accustomed business practices should meet with bitter opposition. Businessmen plead only for certainty in "the rules of the game" and contend that their honest desire to follow the law is thwarted by the confusion into which the law has been plunged by recent court decisions and administrative action. Spokesmen for the Federal Trade Commission, the government agency whose activities have done most to affect the legality of these pricing practices, contend that the confusion is largely of the businessmen's own making, and that the Commission has attempted only to maintain the competitive system of free enterprise through vigorous enforcement of the antitrust statutes.

A lawyer is certain to be rather cautious in attempting to analyze the legal aspects of such a controversial subject which is so intertwined with economic problems and has such an important bearing on business interests. He also naturally is loath to make emphatic statements as to what the law is or will be when the decided cases are relatively few, and reliance must be placed upon what can be properly characterized only as dictum. In such instances he realizes that his opinion is little more than a well-informed guess—sometimes, perhaps, not too well informed. His opinion is apt to be hedged with many "ifs," "buts," and provisos. This accounts, at least in part, for the present conflict and seeming confusion in the expressions of opinion as to the legal status of delivered price systems.

The delivered price systems here considered are of two general types: basing point systems and zone systems. Included in the basing point category are the single basing point, multiple basing point, and freight equalization systems. The freight equalization system is sometimes referred to as the plenary basing point system, as each point of production is a basing point. In basing point systems the delivered price quoted is arrived at by adding to a base price established at some certain plant or geographical point, the freight charge from that point to the buyer's

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destination. The freight charge or factor which is added to the base price may or may not be the actual cost of transporting the article.

The zone systems are of two types: the multiple zone and the single zone, often called the uniform delivered price or universal delivered price system. These systems involve quoting uniform delivered prices within a certain geographic area, which may be as small as a single state, or may include the whole country.

The federal statutes involved in a consideration of the legal aspects of delivered pricing practices are those known as the antitrust statutes. They are the Sherman Act of 1890,[1] the Federal Trade Commission Act of 1914,[2] the Clayton Act of 1914,[3] and the Robinson-Patman Act of 1936[4] which amended Section 2 of the Clayton Act. The legal status of these pricing systems is here considered separately under the several statutes. Although this article attempts to speak only as to the legal aspects of these delivered price systems, it should be pointed out that the solutions to the legal problems involved depend to a great extent upon the results of economic analysis, and an understanding of at least some of the economic aspects of these systems is essential to an understanding of the legal problems.

II

THE SHERMAN ACT

Since the Sherman Act is aimed against monopolies and against contracts, combinations, and conspiracies in restraint of trade, a delivered price system raises problems under this Act only when it is connected in some way with such activities. The principal question in deciding the legality of the delivered price systems under this Act has been whether the system was based on collusive or concerted action in restraint of competition. Therefore, the cases under the Sherman Act involving the use of delivered price systems do not present the issue of the legality per se of these systems. The early cases were decided at a time when the government was first becoming aware of the problem of delivered pricing, and the seeming inconsistency of some of them with later decisions may result from a failure on the part of the prosecution to develop and present its case in an adequate manner. It may of course reflect changes in the membership of the United States Supreme Court since some of these earlier cases were decided, and corresponding changes of judicial thinking on the subject.

The earliest cases which involved the use of a delivered price system to be decided under the Sherman Act belonged to a series in which the "open price" policies of the trade associations were attacked.[5]

[1] 26 STAT. 209 (1890), 15 U. S. C. §1-7 (1946).

[2] 38 STAT. 717 (1914), as amended by 52 STAT. 111 (1938), 15 U. S. C. §41 *et seq.* (1946).

[3] 38 STAT. 730 (1914), 15 U. S. C. §13 (1946).

[4] 49 STAT. 15266 (1936), 15 U. S. C. §13 (1946).

[5] American Column and Lumber Co. v. United States, 257 U. S. 377 (1921); Maple Flooring Ass'n v. United States, 268 U. S. 563 (1925); Cement Mfgrs. Protective Ass'n v. United States, 268 U. S. 588 (1925).

The members of each of the trade associations involved in these cases were using a basing point system to quote delivered prices for their products. In these cases the Supreme Court failed to see any grounds for inferring that the identical prices under the basing point system were the result of understanding, or that the use of the system represented a concerted effort to restrain competition. This may have been because of faulty presentation of the charges by the government, in that it failed in these cases to allege collusive action among the users of the system, and only weakly contended that an inference of collusion or agreement should be drawn from the mechanics of the system and the results of its use.

In the *Maple Flooring* case the Court did indicate that if the basing point system was used to implement an agreement to fix or maintain prices, or if it had produced concerted action to fix or maintain prices, the entire scheme would have been held to be an unlawful restraint of trade.

In the *Cement* case the fact that the Court could view the system as a product of natural growth in a competitive industry seems particularly strange. This would seem to indicate that the government could have made a much better presentation of the economic aspects of the system.

The most important case involving the legality of the basing point system under the Sherman Act to reach the Supreme Court was ***Sugar Institute, Inc. v. United States.***[6]

The lower court held that the concerted maintenance of a basing point delivered price system, which included the concerted use of freight factors which were not the actual cost of delivery, and a refusal to sell f.o.b. refinery, was an unreasonable and illegal restraint of trade. The defendants waived their assignment of error on this point and also on that part of the decree which enjoined concerted action in "determining transportation charges or freight applications to be collected from customers, or limiting freight absorptions; selling only on delivered prices or on any system of delivered prices, including zone prices or refusing to sell f.o.b. refinery."[7]

Although there was present a broad price fixing scheme, the basing point system was not examined merely as one of the devices used to implement the scheme, but was considered apart with respect to the question of whether its concerted use constituted an unreasonable restraint of trade in violation of Section 1 of the Sherman Act. The direct holding of the lower court was that the concerted use of the basing point system was an unreasonable restraint of trade and unlawful.[8] The Supreme

[6] 297 U. S. 553 (1936).

[7] United States v. Sugar Institute, 15 F. Supp. 817, 908 (S. D. N. Y. 1934).

[8] There has been considerable dispute as to whether the court's decision brought the concerted use of a basing point system within the doctrine of per se violations of the Sherman Act, or whether the effect of its use upon competition had to be examined to determine if the restraint on competition was so unreasonable as not to fall within the ambit of the "rule of reason," adopted in Standard Oil Co. of New Jersey v. United States, 221 U. S. 1 (1911).

One line of reasoning is that: "Under this reasoning any agreement to use a basing point system would be unlawful as an agreement to fix a part of the delivered price since the predetermined freight

Court did not pass upon this holding but it did state that, "The unreasonable restraint which defendants imposed lay not in advance announcements, but in the steps taken to secure adherence, without deviation, to prices and terms thus announced."[9] Since the basing point sytem was the means used to secure adherence to the prices announced, this would seem to be an approval of the lower court's conclusion as to the illegality of its concerted use.

There have been two cases involving zone delivered price systems decided by the Supreme Court under the Sherman Act, but in both an agreement or combination in restraint of trade was found on other grounds and the delivered price system was mentioned only incidentally.[10]

The fact that in all these cases arising under the Sherman Act the delivered price system was only one among many activities attacked as restraining trade makes it difficult to spell out any clear conclusions as to the legal status of delivered price systems under the Act. However, it does seem clear from a consideration of these cases that any collusive or concerted use of the basing point system, or any use of

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rates employed are usually higher than necessary, owing to the collection of phantom freight and the quoting of all rail tariffs, and consequently unreasonable. Thus concerted action in maintaining a basing point system, is a type of price fixing." Comment, *Basing Point Pricing and Anti-Trust Policy*, 55 YALE L. J. 558, 574 (1946).

This is, of course, an attempt to bring the concerted use of the basing point system under the per se doctrine as expressed in United States v. Trenton Potteries Co., 273 U. S. 392 (1927), on the theory that there is collusion in fixing the actual delivered price to be charged. In the same article the writer recognizes the most obvious vice of collusive use of the system by remarking that if agreements for uniform price maintenance are illegal, then agreements to adopt a system which necessarily leads to that result should also be declared illegal. The Supreme Court early indicated that agreements for uniform price maintenance are illegal by its statement in the *Cement* case that "agreements or understandings among competitors for the maintenance of uniform prices are of course unlawful." 268 U. S. 588, 604 (1925).

In United States v. American Linseed Oil Co., 262 U. S. 371 (1923), the Court held that a trade association's activities, the fundamental activity being an agreement to adhere to announced prices, necessarily resulted in an illegal restraint of trade. Likewise in this case the Court said that the unreasonable restraints were the steps taken to secure adherence to the prices publicly announced.

Since the decision in United States v. Socony-Vacuum Oil Co., 310 U. S. 150 (1940), there seems to be no room to dispute that agreements to maintain identical prices or to adhere to announced prices are illegal. Since the purpose and necessary result of the concerted used of a basing point system is the maintenance of identical delivered prices at all points, and adherence to the announced base price is an essential part of the concerted action, it necessarily follows that an agreement to use the basing point system is a per se violation of the Sherman Act.

The Federal Trade Commission had this to say about collusive use of the basing point system: "Where the geographic pricing formula is significantly involved, its importance springs from the fact that it is used as a price fixing device and that analysis of its operation provides evidence that there has been a collusive agreement. It is always possible for businessmen, instead of agreeing to prices directly, to agree instead that they will all use a formula which has the effect of making their prices identical." FTC, NOTICE TO THE STAFF: IN RE: COMMISSION POLICY TOWARD GEOGRAPHIC PRICING PRACTICES (Oct. 12, 1948).

All do not agree that concerted use of the system is a per se violation, however: "Even assuming the existence of a combination to use the basing point system, it must still be decided whether the combination constitutes an unlawful restraint upon trade." Note, *Multiple Basing Point Pricing in the Cement Industry*, 42 ILL. L. REV. 364, 369 (1947). See also Note, *Anti-Trust Law—Cement Industry—Legality of Multiple Basing Point Pricing System*, 95 U. OF PA. L. REV. 408 (1947).

[9] Sugar Institute, Inc. v. United States, 297 U. S. 553, 601 (1936).

[10] Standard Sanitary Mfg. Co. v. United States, 226 U. S. 20 (1912); United States v. American Linseed Oil Co., 262 U. S. 371 (1923).

the system to facilitate or effectuate any agreement, conspiracy, understanding, or concerted action with respect to prices is such a restriction and restraint on competition as to be unlawful under Section 1 of the Sherman Act. There seems to be no peculiar characteristic of the basing point system which should lead us to think that the same rule would not be applicable to the other delivered price systems, although there is a paucity of authority in the form of decided cases to support such a conclusion.[11]

III

THE FEDERAL TRADE COMMISSION ACT

It has been the action of the Federal Trade Commission which has done most to clarify or, as some would have it, to confuse the legal status of delivered price systems. The Commission has proceeded against such systems both under the Federal Trade Commission Act and the amended Clayton Act. Here we will consider only its action under the former statute.

The Commission is given authority by the Federal Trade Commission Act to prevent the use of unfair methods of competition in interstate commerce. The Commission has proceeded against agreements or combinations in restraint of trade as constituting unfair methods of competition within the meaning of the Act, and it has been definitely decided by the Supreme Court that the term "unfair methods of competition" in Section 5 of the Federal Trade Commission Act includes violations of the Sherman Act.[12] Most of the Commission's proceedings against delivered price systems have been based upon charges of activity which would also be illegal under the Sherman Act. These cases are based upon charges that the delivered price system is being collusively used as a price fixing device. Since a concerted or collusive use of a delivered price system, or use of the system to effectuate any agreement, conspiracy, understanding, or concerted action with respect to prices is unlawful under the Sherman Act, it is the manner in which the Commission has proved such use of the system that is of particular significance here.

The Commission's method of proving prohibited use of the delivered price systems has been the main object of criticism directed against it in its proceedings under the Federal Trade Commission Act. The Commission has been accused of assuming that wherever a delivered price system has been used by several sellers there has been a conspiracy or concerted action to adopt or maintain the system.[13]

[11] In this connection it should be noted that the decree in the *Sugar Institute* case enjoined concerted action in "selling only on delivered prices or on any system of delivered prices including zone prices or refusing to sell f.o.b. refinery." 15 F. Supp. 817, 908 (S. D. N. Y. 1934).

[12] Federal Trade Comm'n v. Pacific States Paper Trade Ass'n, 273 U. S. 52 (1927), was the first case in which the Supreme Court upheld the Commission's authority to proceed against price fixing as an unfair method of competition. Many cases have indicated that "unfair methods of competition" embraced all Sherman Act violations, but in Federal Trade Comm'n v. Cement Institute, 333 U. S. 683, 690 (1948), the Court directly held that this was the case.

[13] "It is recognized that aggressive competition may result in a virtual identity of prices. It is also suggested that an unlawful price conspiracy will achieve price identity. Yet the committee will discover that a considerable part of the present uncertainty flows from the insistence of Government, and par-

It must be remembered, however, that an order under the Act does not require a finding of a conspiracy or combination to restrain trade. Practices which have a dangerous tendency unduly to hinder competition or create monopoly have been held to be "unfair methods of competition," irrespective of the presence of conspiracy or combination.[14] This principle has been applied to the delivered price field in only a very few instances, but as we shall see its relevancy there has been favorably passed upon by the Supreme Court. It is through this principle that we are most likely to get a determination of the issue of the legality per se of the various delivered price systems under the Federal Trade Commission Act.

The Federal Trade Commission's fight against delivered price systems started with its proceeding in 1924 against the United States Steel Corporation and its subsidiaries. The respondents were using a single basing system of pricing which utilized Pittsburgh as a basing point. They sold their rolled steel at the Pittsburgh base price plus freight from Pittsburgh to destination, regardless of the location of the actual shipping point. Steel manufacturers near Birmingham, Alabama sold with Birmingham as a base point. The base price at Birmingham was made up of the Pittsburgh base plus a purely arbitrary differential of $5.00 per ton. The Commission charged that respondents by use of this pricing system discriminated in price among their customers in violation of Section 2 of the Clayton Act, and that this use constituted an unfair method of competition under Section 5 of the Federal Trade Commission Act.

The Commission's findings were that the use of the Pittsburgh plus system resulted in price discriminations which substantially lessened competition among consumers of steel, between respondents and other consumers of steel who were forced to pay the discriminatory prices, and among all producers of steel in the United States, as all producers followed the Pittsburgh plus system of the respondents. It found further that such a use of this system was an unfair method of competition. The respondents were ordered to cease and desist from selling their products on the Pittsburgh plus basis and from selling upon any other basing point than that where the products were manufactured or from which they were shipped. On September 17, 1924, the respondents filed a report with the Commission stating their intention of complying with the order "in so far as it is practicable to do so."

The respondents, however, did not comply with this order, but adopted a multiple basing point system of pricing instead.[15] Then in 1938 the Wheeler-Lea

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ticularly administrative officials, in assuming that where substantial price identity is found there must have been a conspiracy in fact." John M. Hancock, in *Hearings before Subcommittee of the Committee on Interstate and Foreign Commerce on S. Res. 241*, 80th Cong., 2d Sess. 9 (1948).

"What should be painstakingly considered by the courts is the Commission's position, as revealed in its proceeding against the Cement industry . . . that the nature of the basing point system is such that it is never used except for the purpose of collaborating with other sellers. . . ." Hilder, *The Attack Upon Delivered Price Systems*, 14 GEO. WASH. L. REV. 397, 420 (1946).

[14] Federal Trade Comm'n v. Gratz, 253 U. S. 421, 427 (1919); Federal Trade Comm'n v. Beech-Nut Packing Co., 257 U. S. 441 (1921); United States Steel Corp., 8 F. T. C. 1 (1924).

[15] A. R. BURNS, THE DECLINE OF COMPETITION 306 (1938).

amendment[16] to the Federal Trade Commission Act made the decree of the Commission final if the respondent fails to petition a circuit court of appeals to review it. This caused the steel companies to file a petition for review in the Circuit Court of Appeals for the Third Circuit. The case remained pending until after decision of the *Cement* case in 1948. The issues in the case were narrowed by the filing of a brief by the steel companies which was claimed to be essentially a request that the petitioners be allowed to absorb freight to meet competition. On July 10, 1948, the Commission filed its brief on this question. An important statement in that brief was:[17]

> But the oppressive nature of the practice is not confined to so-called phantom freight. If every point of shipment were to be made a basing point and all phantom freight eliminated, the system would still be oppressive to the various purchasers in that those at or near the factory door would have to pay more to that factory in order that its distant purchasers might pay less. Such is the effect of systematic freight absorption. Such is the practice that must be appraised in the light of the Supreme Court's declaration in the *Staley* case that a nondiscriminatory pricing system was one giving to purchasers, who have the natural advantage of proximity to its plant, "the price advantages which they are entitled to expect over purchasers at a distance." Federal Trade Commission v. Staley Mfg. Co., 324 U. S. 746, 757.

This statement was made to support a contention that a method of competition is unfair if it involves oppression. The argument is that the discrimination inherent in the use of a basing point system is oppressive toward the nearby customers who pay the high net prices, as they in effect subsidize the cost of transportation to the more distantly located buyers. This is not a new contention, however, as such discrimination against buyers by the petitioners was found to be an unfair method of competition in the original proceeding.

It is true of course that the Commission made findings in the original proceeding that there was collusion between respondents and other steel producers to use the pricing system, and even though there was no allegation of collusion in the charge there was a charge which in effect alleged that the respondents' use of the system with knowledge that other producers would use it constituted an unfair method of competition because of its effect on competition among all steel producers.[18] This charge was aimed at the same type of injury to competition that would result from a price fixing conspiracy, and as we shall see is practically the

[16] 52 STAT. 111 (1938), 15 U. S. C. §45 (1946).

[17] Brief for Appellees, United States Steel Corp. v. Federal Trade Comm'n, Docket No. 6796 (C. C. A. 3d 1938).

[18] The actual allegation was that the effect of respondents' use of the system was "to substantially lessen competition among all the producers of the said steel in the United States . . . as all producers of steel in the United States adhere to the Pittsburgh Plus system and without the maintenance by respondents of the said Pittsburgh Plus, and the said Birmingham price, the other producers of said rolled steel in the United States would be unable to maintain said prices." United States Steel Corp., 8 F. T. C. 1, 9 (1924).

The Commission found that the purpose of the system was to allow all producers to match each others' prices.

same as the second count in the *Conduit* case.[19] The Commission in its recent brief in this case again asserts that this common or parallel use of the basing point system is an unfair method of competition because its effect is indistinguishable from a conspiracy to fix prices.[20]

This charge against the common use of the system is obviously the basis for the contention that the Commission has never proceeded against the basing point system under the Federal Trade Commission Act except where it was used in concert, and that there is no reason to suppose that it will, to be drawn from this or other delivered price cases.[21] The fact that the Commission did find in this case that respondents' discrimination in price was an unfair method of competition, when coupled with the argument set out in the Commission's brief that the discrimination against the nearby buyers, which is inherent in systematic freight absorption, is an unfair method of competition, does not leave one too assured that the Commission will not proceed against an individual seller's use of the basing point system under Section 5 of the Federal Trade Commission Act regardless of the incidence of the system in the industry. Since the order of the Commission in this case was never reviewed by a court, but a consent decree entered,[22] the precedent value of the case is weak, although it is valuable to show the Commission's attitude toward delivered price systems and its method of attacking them.

The Commission's argument that the individual use of a basing point system is an unfair method of competition because it is oppressive seems to be based upon the old case of *Federal Trade Commission v. Gratz*.[23] This case involved a proceeding by the Commission against a seller of cotton ties who refused to sell the ties unless the purchaser also took a certain amount of jute bagging. The Supreme

[19] Triangle Conduit and Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *aff'd per curiam sub nom.* Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949).

[20] "The basing point system here used creates a dangerous tendency unduly to hinder competition and create monopoly by providing a device that automatically results in identical delivered prices and makes it impossible for buyers to find any price advantage in choosing among rival sellers. In other words, to the extent the basing point system here is followed, it produces the very same effect upon prices and price competition that would be produced by a combination and conspiracy to fix prices. Thus the system has more than a dangerous tendency to unduly hinder price competition. It precludes price competition *per se*." Brief for Appellees, United States Steel Corp. v. Federal Trade Comm'n, Docket No. 6796 (C. C. A. 3d 1938).

[21] "The Commission emphasizes the basing point system if it is so complicated, so rigid, and so contrary to competitive common sense in its results, that its continued existence gives persuasive evidence of the existence of the collusion, and if it is so central that its abandonment would be likely to destroy the collusion. . . . There is no instance in which the Commission has charged that a single company using a basing point system without regard to what its competitor is doing is in violation of the Federal Trade Commission Act." Corwin D. Edwards, Director, Bureau of Industrial Economics, F. T. C., in a speech delivered at a technical seminar sponsored by the Department of Commerce for state planning and developing agencies, Washington, D. C., August 4, 1948.

"The Commission has never brought a proceeding charging that freight absorption by a single seller, not accompanied by reciprocal absorption by others violates the Federal Trade Commission Act. Nor is there any reason for believing that the Commission will change its policy and make freight absorptions of this kind the target of proceedings under the Trade Commission Act." Herbert A. Bergson, Ass't Attorney General, Antitrust Division, Department of Justice, *Hearings, supra* note 13, at 99.

[22] United States Steel Corp., Docket No. 760 (C. C. A. 3d 1948).

[23] 253 U. S. 421 (1919).

Court affirmed the circuit court's ruling which annulled the Commission's order, solely on the ground that the complaint did not show unfair competition. The only reference to oppression by the Court was its statement as to the meaning of the words "unfair method of competition."[24] This was only a very general reference as to the possible application of the concept of unfair methods of competition and is but scant support for the Commission's argument. Whether the "oppression" which the Commission found to be inherent in the use of a basing point system by a single seller would be such as to constitute an unfair method of competition is completely unsettled, and no good authority to support the contention can be cited.

If denial to the buyer of this "natural advantage of proximity to the plant" should be considered an unfair method of competition because oppressive, then every delivered price system which we are considering would be unlawful under the Federal Trade Commission Act, as this "oppression" is inherent in these systems. As will be seen when the problems arising under the Clayton Act are considered, it has never been held that denial of this "advantage" has the defined statutory effect upon competition in the second line, and the Commission has intimated that only collusive or common denial of this right is considered illegal. If the effect of this practice is not such as to constitute a violation of the Clayton Act it is doubtful if it would be held a violation of the Federal Trade Commission Act, although one member of the Commission, Allen C. Phelps, asserted that if the *Conduit* case was upheld in the Supreme Court, "We have now arrived at the point where a violation of the Robinson-Patman Act is also an unfair method of competition, and following the reasoning of the Supreme Court in the *Cement* case, unfair methods of competition may include price discriminations which fall short of violations of the Robinson-Patman Act."[25]

This assertion is based upon the fact that it was held in the *Conduit* case that conspiracy was not necessary to a finding of violation of the Federal Trade Commission Act, if the conduct had the same effect upon competition as a conspiracy. This holding does not support the assertion, however, as it contemplates the same effect upon competition, whereas Mr. Phelps' statement would include situations in which the defined statutory effect on competition was not present.

In view of the great reliance which the Supreme Court has recently placed upon the "expertness" of the Federal Trade Commission it is not inconceivable that this view if pressed will be sustained. However, after its brief was filed in the *United States Steel* case, the Federal Trade Commission indicated that it had abandoned this argument.[26] The Commission was not so quick to abandon its argument that

[24] "The words 'unfair method of competition' are not defined by the statute, and their exact meaning is in dispute. It is for the courts, not the commission, ultimately to determine, as matter of law what they include. They are clearly inapplicable to practices never heretofore regarded as opposed to good morals because characterized by deception, bad faith, fraud, or oppression, or as against public policy because of their dangerous tendency unduly to hinder competition or create monopoly." *Id.* at 427.

[25] *Hearings, supra* note 13, at 133.

[26] "The problem created by freight absorption under the Federal Trade Commission Act arises, however, only where the result of the practice is the elimination of price competition. Freight absorption

conscious parallel use of a basing point system with reciprocal freight absorptions is an unfair method of competition, however, and as we shall see in our discussion of later cases this contention seems to rest upon a much sounder foundation than its arguments as to the oppression involved in the single seller's use of the system.

The Federal Trade Commission's other proceedings under Section 5 of the Federal Trade Commission Act have been confined largely to conspiracy cases in which there has been found an agreement to use the system or where the system has been found to be used as the means of effectuating an agreement or understanding on prices. Under Section 5 the Commission has entered orders against basing point conspiracies in several proceedings involving various industries.[27]

The first of such cases to be reviewed by the courts was *United States Maltsters Association v. Federal Trade Commission*.[28] The complaint, directed against eighteen malt manufacturers and their trade association, charged that they had entered into an "agreement, combination, understanding and conspiracy among themselves to fix and maintain, and by which they have fixed and maintained uniform delivered prices. . . ."[29]

The Commission found that the Trade Association received reports from the members as to malt sales showing date, destination of shipment, grade and quantity of malt sold, and price received f.o.b. Chicago basis. This information was compiled by the association and distributed to the members. The Commission found further that, pursuant to agreement, whenever a member changed his price to a customer he notified the association of the new price immediately; such information was then relayed by the association to the other members.

The Commission also found an agreement to use a compilation of freight rates based upon Chicago as a base in order to compute delivered prices, to use uniform grading standards, to quote delivered prices only, to use standard seller's contracts only, and to adopt uniform discounts. It concluded that by means of these agreements and conspiracies respondents had "agreed to fix and maintain and did fix and maintain, the delivered price of malt,"[30] and that this uniformity of delivered prices was achieved by use of the single basing point system.

The sole issue in the case on review was whether the findings of the Federal Trade Commission were supported by competent evidence. The court of course refused to weigh the evidence and said, "Our function is limited solely to an in-

by a single seller, not accompanied by the reciprocal absorptions by others, raises no problem under the Federal Trade Commission Act." FTC, STATEMENT OF POLICY, *supra* note 8.

[27] Pine Hill Lime and Stone Company, 33 F. T. C. 427 (1941); The Hardwood Institute, 34 F. T. C. 661 (1942); The Cement Institute, 37 F. T. C. 87 (1943); United States Maltsters Ass'n, 35 F. T. C. 797 (1942), modified, 37 F. T. C. 419 (1943); The Milk and Ice Cream Can Institute, 37 F. T. C. 419 (1943); Rigid Steel Conduit Ass'n, 38 F. T. C. 534 (1944); Ferro Enamel Corporation, 42 F. T. C. 36 (1946); American Refractories Institute, No. 4900, April 13, 1948; Crown Manufacturers Ass'n of America, No. 5814, August 4, 1948.

[28] 35 F. T. C. 797 (1942), 152 F. 2d 161 (C. C. A. 7th 1945).

[29] 35 F. T. C. 797, 800 (1942).

[30] *Id.* at 809.

quiry as to whether the record furnishes substantial support for such findings."[31] In holding that the Commission's findings were supported by substantial, competent evidence the court made certain statements which would lead one to believe that the Commission relied heavily upon the mere existence of the basing point system and the resulting identical delivered prices to support its charge of a conspiracy to fix and maintain prices.[32] The truth is, however, that the court went much further than the Commission in attaching significance to the mere existence of the delivered price system. The Commission showed enough evidence of concerted activity to facilitate the basing point system to support a finding of agreement to adopt and maintain the system. It necessarily follows, therefore, that its findings of conspiracy to fix and to maintain prices were amply supported.[33] The court's opinion might be important as showing that it would accept a finding of conspiracy based solely upon proof of the use of the basing point system.

Another important basing point case to reach the courts was the *Milk and Ice Cream Can* case.[34] This is the first case involving a freight equalization plan to be reviewed. Respondents were the manufacturers of milk and ice cream cans and their trade association, the Milk and Ice Cream Can Institute. A reporting system was employed by which the members' activities, including prices received from sales, were daily made known to the Institute. The Institute members used a freight equalization plan implemented by the use of a freight rate book which made it possible to compute and quote freight rates on an equalized basis. This rate book was furnished to the members by the Institute, and the Commission found that there was an agreement to use this book in calculating the delivered price quotations. It found further that the Institute established a classification of buyers with a determined discount allowable to each class.

The Commission found that the freight equalization plan was used pursuant to an agreement or understanding and was the device used to carry out a conspiracy to fix and maintain delivered prices. These findings were based upon a showing of the existence of the system and the several joint activities which were employed to facilitate and carry it out. Here again, however, as in the *Maltsters* case, the

[31] United States Maltsters Ass'n v. Federal Trade Comm'n, 152 F. 2d 161, 162 (C. C. A. 7th 1945); Section 45(c) of the Federal Trade Commission Act provides: "The findings of the Commission as to the facts, if supported by evidence, shall be conclusive." 38 STAT. 719 (1914), as amended, 52 STAT. 111 (1938), 15 U. S. C. §45 *et seq.* (1946).

The courts have described the quantum and quality of evidence necessary to support the Commission's findings in such a way that there is confusion as to just what evidence is required. It is useless, however, to speculate as to the theoretical differences of these varying descriptions, and space limitations forbid an extended examination of the cases. It does seem safe to say that the Supreme Court is displaying in these delivered price cases a greater respect for the "expertness" of the Commission, and its findings are apt to be conclusive unless clearly arbitrary and unreasonable.

[32] "We are of the view that the Commission's findings that a price fixing agreement existed must be accepted. Any other conclusion would do violence to common sense and the realities of the situation. The fact that petitioners utilized a system which enabled them to deliver malt at every point of destination at exactly the same price is a persuasive circumstance in itself." United States Maltsters Ass'n v. Federal Trade Comm'n, 152 F. 2d 161, 164 (C. C. A. 7th 1945).

[33] See note 8 *supra*.

[34] Milk and Ice Cream Can Institute v. Federal Trade Comm'n, 152 F. 2d 478 (C. C. A. 7th 1946).

language of the court could be interpreted to mean that conspiracy could be proved by showing merely that the pricing system was in use and produced identical delivered prices.[35]

The next basing point case to reach the courts on review has occasioned more comment than all the others combined. It has put the delivered price problem on the front page, and into the thoughts of most American businessmen, and was the principal reason for the launching of the Congressional investigation of the delivered price problem.[36] This, of course, is the *Cement* case.[37]

In 1937 the Federal Trade Commission filed a complaint against the seventy-five major cement manufacturers and their trade association, the Cement Institute, charging that the respondents had restrained and hindered competition in the sale and distribution of cement by means of a combination among themselves made effective through the mutual understanding or agreement to employ a multiple basing point system of pricing. This was alleged to be an unfair method of competition in violation of Section 5 of the Federal Trade Commission Act, and to result in systematic price discriminations between the customers of each respondent in violation of Section 2 of the amended Clayton Act. The Commission found that these charges were supported by competent evidence and issued its cease and desist order in 1943, which ordered respondents to cease and desist from "carrying out any planned common course of action, understanding, agreement, combination or conspiracy"[38] to do certain things. The Commission contended that these things had to be restrained to restore individual freedom of action among the different units in the cement industry.

The Commission's order was vacated in 1946 by the United States Court of Appeals for the Seventh Circuit.[39] The Supreme Court granted certiorari in March, 1947, and in April, 1948, handed down its decision reversing the circuit court and affirming the order of the Federal Trade Commission. For the present we shall consider only the first count of the Commission's complaint: that charging violation of Section 5 of the Federal Trade Commission Act.

The action of the seventh circuit court is all the more surprising when it is recalled that this is the same court that decided the *Maltsters* and *Ice Cream Can*

[35] "On the face of the situation, it taxes our credulity to believe as argued that petitioners employed the system without any agreement or plan among themselves." *Id.* at 482. "The mere fact that the situation did exist in and of itself furnishes strong support that the Institute and its members were acting cooperatively and by agreement." *Id.* at 487.

Mr. Lynn C. Paulson, Assistant Chief Trial Counsel of the F. T. C., pointed this out in his testimony before a Senate Committee:

"Senator, I think we have been injured a time or two by voluntary statements from various courts. They have volunteered in the *Milk Can* case and the *Crepe Paper* case, saying this would be conspiracy whether or not there were any facts. We haven't proceeded on that basis. We have always gone to the facts and have not needed or have not used voluntary statements by the courts." *Hearings, supra* note 13, at 122.

[36] S. Res. 241, 80th Cong., 2d Sess. (1948).

[37] Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948).

[38] 37 F. T. C. 87, 258-266 (1943).

[39] 157 F. 2d 533 (C. C. A. 7th 1946).

cases, the same judge (Major) writing the majority opinion in this and the other two cases. This court held that there was not sufficient evidence to support a Commission finding of a combination among the respondents to restrain competition in price as was charged in both counts of the complaint. Doubt was expressed that the findings of the Commission would support the charge of combination even if supported by sufficient evidence in the record.

In attempting to distinguish this case from the *Maltsters* and *Ice Cream Can* cases the circuit court revealed that it saw nothing illegal in an agreement to employ a basing point system, and that it failed to realize that in these prior cases the Commission's findings of conspiracy to fix prices were based upon its belief that concerted adherence to a formula which produced identical delivered prices was a conspiracy to fix and maintain prices.[40]

The dissenting judge in the circuit court recognized that the Commission's charge was directed against agreed-upon use of the basing point system.[41] He also felt that the majority opinion deviated from the court's prior decisions on the subject and that the majority was forgetting that the Commission and not the court was the fact finder.

The Supreme Court, in reviewing the case, first overruled the respondents' contentions that the Federal Trade Commission Act did not embrace violations of the Sherman Act,[42] and then found that the Commission had made adequate findings of a combination to utilize the basing point system as a means of suppressing price competition.[43] As to the sufficiency of these findings, the Court remarked:[44]

[40] "The Commission also relies strongly upon the recent decisions of this court in *U. S. Maltsters Ass'n v. F. T. C.*, and *Milk and Ice Cream Can Institute v. F. T. C.*, in support of its contention that identical delivered prices are evidence of conspiracy or concerted action. We need not discuss these decisions any further than to point out that in each of those cases a conspiracy to fix prices was charged and found. The multiple basing point price system was not directly involved in either case. In other words, the conspiracy was to fix prices and not merely to use a system from which uniformity of prices resulted, as in the instant case and the old Cement case." *Id.* at 572.

[41] "The Commission's challenge here lays stress on the agreement to utilize a multiple basing point system per se and its order is correspondingly limited to such asserted illegal agreement." *Id.* at 575 (Judge Evans dissenting).

[42] See note 12 *supra.*

[43] "The Commission's findings of fact set out at great length and with painstaking detail numerous concerted activities carried on in order to make the multiple basing point system work in such a way that competition in quality, price and terms of sale of cement would be nonexistent, and that uniform prices, job contracts, discounts, and terms of sale would be continuously maintained. The Commission found that many of these activities were carried on by the Cement Institute, the industry's unincorporated trade association, and that in other instances the activities were under the immediate control of groups of respondents. Among the collective methods used to accomplish these purposes, according to the findings, were boycotts; discharge of uncooperative employees; organized opposition to the erection of new cement plants; selling cement in a recalcitrant price cutter's sales territory at a price so low that the recalcitrant was forced to adhere to the established basing point prices; discouraging the shipment of cement by truck or barge; and preparing and distributing freight rate books which provided respondents with similar figures to use as actual or 'phantom freight' factors, thus guaranteeing that their delivered prices (base prices plus freight factors) would be identical on all sales whether made to individual purchasers or under sealed bids. These are but a few of the many activities of respondents which the Commission found to have been done in combination to reduce or destroy price competition in cement." 333 U. S. 683, 709-710 (1948).

[44] *Id.* at 712.

It seems impossible to conceive that anyone reading these findings in their entirety could doubt that the Commission found that respondents collectively maintained a multiple basing point delivered price system for the purpose of suppressing competition in cement sales.

The Court also overruled respondents' contention that the Commission's finding of combination was not supported by substantial evidence. In so doing the Court pointed to the many practices engaged in by the respondents to facilitate and maintain the basing point system, such as the boycotting of dealers who sold imported cement, pledges by producers not to sell f.o.b. plant, and the establishment of a punitive basing point to punish recalcitrants, and observed:[45]

The Commission was authorized to find understanding, express or implied, from evidence that the Industry's Institute actively worked, in cooperation with various of its members, to maintain the multiple basing point delivered price system; that this pricing system is calculated to produce, and has produced, uniform prices and terms of sale throughout the country; and that all of the respondents have sold their cement substantially in accord with the pattern required by the multiple basing point system.

This is a direct approval by the Supreme Court of the Commission's method of proving a concerted use of the basing point system, that is, proof of the use of the system and of the various practices which are always employed to maintain the system. This is, it is true, not a holding that such a system is illegal per se, but since it is very unlikely that such a system could be maintained among several sellers without the use of at least some of these cooperative implementations,[46] the system when so used will probably be unable to withstand a charge of conspiracy.

As to the legality of a conspiracy or agreement to use the multiple basing point system the Court had this to say:[47]

We sustain the Commission's holding that concerted maintenance of the basing point delivered price system is an unfair method of competition prohibited by the Federal Trade Commission Act.

The Court then added a statement which, although admittedly dictum, might well prove to be its most important pronouncement in the entire case, particularly in view of the next case which we shall consider:[48]

While we hold that the Commission's findings of combination were supported by evidence, that does not mean that existence of a "combination" is an indispensable ingredient for an unfair method of competition under the Trade Commission Act.

[45] *Id.* at 716.

[46] "It is conceivable that a basing-point cartel may function without any visible tools or gadgets, without any trace of patently collusive acts, without any 'cartel organs' aiding the observance of unwritten 'cartel rules.' Theoretically, the publication of base prices by the basing point mills is the only indispensable device for the operation of the system. This, however, is not likely to work in practice, at least not over a long period." F. MACHLUP, THE BASING POINT SYSTEM 20 (1948).

"This is particularly apparent as to basing point systems, which seem necessarily to require collusion, either in outright form or in 'parallel action' of a sort which will not withstand the inference of collusion." Wright, *Collusion and Parallel Action in Delivered Price Systems*, 37 GEO. L. J. 201, 213 (1948).

[47] 333 U. S. 683, 720 (1948).

[48] *Id.* at 721.

Justice Burton wrote a dissenting opinion very similar to the majority opinion in the circuit court.

The *Conduit* case[49] was the next basing point proceeding to be reviewed by the courts. The petitioners were fourteen manufacturers of rigid steel conduit who sought to have set aside a cease and desist order of the Federal Trade Commission based upon a complaint in two counts, which charged a collective violation by the petitioners and their trade association, the Rigid Steel Conduit Association, of Section 5 of the Federal Trade Commission Act.

The first count alleged that petitioners were engaged in a conspiracy whose purpose and effect was to restrict and suppress actual and potential competition in the distribution and sale of rigid steel conduit in commerce, and which was effectuated by the adoption and use of a basing point method of quoting prices. This count is similar to the first count in the *Cement* case and was sustained by the Commission upon evidence much like that adduced in that case. The use of the system and the various cooperative practices employed to maintain it were shown. The principal implementation activities were compilation of freight adders to insure identical delivered price quotations, classification of customers and establishment of differentials between them, adoption of uniform contracts, and investigations to enforce compliance with such contracts. The court said that there *was* direct proof of the conspiracy but even if there was not, "in determining if such a finding is supported it is not necessary that there be direct proof of an agreement. Such an agreement may be shown by circumstantial evidence."[50]

The second count did not depend upon combination or conspiracy. It charged that each respondent with knowledge that the other respondents did likewise, refrained from quoting f.o.b. prices, but computed prices by use of the basing point formula which resulted in a price made up of the published price plus freight adders from one or more basing points, despite the fact that shipment might actually be made from some other point from which some other freight factor might actually apply. Uniformity in the delivered prices of respondents at a given destination was alleged to be "inherent in, and a necessary result of, such method or system of basing-point-delivered-price quotations."[51]

It was alleged further that respondents habitually charged their customers located near their plant a higher price than those located at a distance, thus forcing the nearby customers to pay more and the customers at a distance "within and without a particular basing point area to pay less, than would otherwise be the case, thus depriving the nearby customers of each said respondent 'conduit seller' of price advantages which they would naturally enjoy by reason of their proximity to points of production."[52]

[49] Triangle Conduit and Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *aff'd per curiam sub nom.* Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949).

[50] 168 F. 2d 175, 180 (C. C. A. 7th 1948).

[51] Rigid Steel Conduit Ass'n, 38 F. T. C. 534, 550 (1944).

[52] *Ibid.*

The Commission found that the use of the basing point system produced the results alleged[53] and concluded that these acts and practices constituted unfair methods of competition in violation of Section 5 of the Federal Trade Commission Act.

The court, in considering the second count, pointed out the conscious parallel use of the basing point formula, the matching of prices, and the systematic variations in mill nets of the sellers, and said:[54]

> Each seller consciously intends not to attempt the exclusion of any competitor from his natural freight advantage territory by reducing the price, and in effect invites the others to share the available business at matched prices in his natural market in return for a reciprocal invitation.

It then stated that the legal issue presented was the same as in the *Cement* case; referred to the Supreme Court's dictum that a combination is not necessary to the finding of an unfair method of competition; and concluded, "In the light of that opinion, we cannot say that the Commission was wrong in concluding that the individual use of the basing point method *as here used* does constitute an unfair method of competition."[55]

The Supreme Court affirmed the decision of the circuit court, but unfortunately without any written opinion.[56]

There has been much discussion and some dispute as to the meaning and breadth of the court's holding on the second count in this case. Some seem to think that the phrase "as here used" means that the Court never really passed upon the legality of an individual use of the system with knowledge that others are using it, and that the holding is based upon conspiracy or collusion.[57]

The Federal Trade Commission itself has issued several statements on the meaning of the *Conduit* case. In one press release the Commission interpreted the case as holding the basing point method of pricing to be an unfair method of competition regardless of conspiracy.[58] On October 12, 1948, the Commission issued a statement of policy designed to explain and further clarify the law which pointed

[53] The Commission also found: "That the capacity, tendency, and effect of the use by each respondent named therein of the basing point delivered-price formula to determine price quotations and prices which will be made to conduit purchasers at any given destination concurrently with similar use of the same pricing formula by other of the said respondents has been, and is, to hinder, lessen, and restrain competition in price in the sale and distribution of conduit; to deprive purchasers of the benefits of competition; to create in each of said respondents a dangerous tendency toward a monopolistic control over price in the sale and distribution of conduit." *Id.* at 593.

[54] 168 F. 2d 175, 181 (C. C. A. 7th 1948).

[55] *Ibid.* (Italics supplied.)

[56] 336 U. S. 956 (1949).

[57] "I think if I were advising a client I would say 'as here used,' and that means pursuant to a combination and conspiracy. I think I would take that gamble if I were advising a client. That remains to be settled, I think." Lynn C. Paulson, Ass't Chief Trial Counsel, F. T. C., *Hearings*, *supra* note 13, at 241.

[58] "Use of a basing point system of delivered prices by individual companies, engaged in the production and sale of rigid steel conduit, with knowledge that other sellers are using the same pricing methods and with the result that price competition is unreasonably restrained constitutes an 'unfair method of competition' in violation of the Federal Trade Commission Act irrespective of any combination or conspiracy." F. T. C. Press Release, May 19, 1948.

out that, although the Commission thought that the economic results flowing from a number of sellers following a parallel course of action were the same as those flowing from a combination or conspiracy, it did not base its Count II upon any combination or conspiracy.[59]

It seems quite clear therefore that the Commission did not rely upon combination or conspiracy under Count II. In fact it was careful to point out in its brief that it did not do so, saying:[60]

> Under Count II the issue is simply whether the concurrent use of the basing point practice—constitutes . . . an unfair method of competition within the meaning of Section 5 of the Federal Trade Commission Act.

In still another place in its brief the Commission stated:[61]

> Count II and a corresponding part of the order are frankly directed against the basing point practice as being *per se* an unfair method of competition, even though not predicated on combination and conspiracy.

In fact, to construe this second count of the case as based upon the conspiracy found under the first count is to make it meaningless and mere surplusage.

This is the second instance, the *Pittsburgh Plus* case being the first, in which the Commission has found that where there is common use of the basing point system in an industry, each seller's adherence to and employment of the system is an unfair method of competition. This finding is based upon the realization that common and reciprocal use of a basing point system, whether induced by agreement, price leadership, or what not, produces the same economic results and has the same destructive effects upon price competition.[62] That the count was phrased in this way, instead of charging conspiracy or combination, illustrates also the Commission's belief that it had need for this type of complaint in order to secure effective relief from the collusive conduct proved in the first count.[63]

[59] "In the *Rigid Steel Conduit* case, the Commission found, and the circuit court agreed, that adherence to an industry-wide basing point formula, with the knowledge that other concerns are adhering to it also constitutes in itself a violation of the Federal Trade Commission Act by the individual adhering companies when price competition is thereby eliminated. It would have been possible to describe this state of facts as a price fixing conspiracy on the principle that when a number of enterprises follow a parallel course of action in the knowledge and contemplation of the fact that all are acting alike, they have in effect, formed an agreement. Instead of phrasing its charge in this way, the Commission chose to rely on the obvious fact that the economic effect of identical prices achieved through conscious parallel action is the same as that of similar prices achieved through overt collusion, and, for this reason, the Commission treated the conscious parallelism of action as a violation of the Federal Trade Commission Act." FTC, STATEMENT OF POLICY, *supra* note 8.

[60] Brief for F. T. C., Triangle Conduit and Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948).

[61] *Ibid.*

[62] "Even this charge rests upon a concert of action which brings about an economic effect indistinguishable from the collusion which is also charged in the same complaints." Corwin D. Edwards, *supra* note 21.

[63] "It prohibits them from continuing the same kind of practice that they had formerly continued by means of a conspiracy. . . . It is founded basically upon the proved and established injury to the competition in the past and upon the practically certain continuation of that injury in the future." W. B. Wooden, Associate General Counsel and Chief, Division of Appellate Proceedings, F. T. C., *Hearings*, *supra* note 13, at 695.

Although the second count is not based upon combination or collusion but upon conscious parallelism of action, the principle developed will probably have application only in situations in which actual conspiracy could be proved. Consequently, its principles have no application to the question of the legality of the independent use of the basing point system by a single seller, or the legality of such seller's practice of absorbing freight.[64]

The Commission bases its method of proceeding under this second count primarily upon the *Beech-nut* case,[65] and upon the dictum in the *Cement* case that combination is not necessary to an unfair method of competition within the meaning of the Federal Trade Commission Act. In the *Beech-nut* case the Court upheld the Commission's order against the respondent's price-maintenance policy—because of its tendency unduly to hinder competition or create monopoly even though the complaint was not based upon combination or collusion.[66] In this case, however, there was evidence adduced from which an actual agreement probably could have been inferred. It is, therefore, somewhat misleading to attempt to support the conscious parallelism of action theory of the second count by means of the *Beech-nut* case. Likewise, the principle that combination or conspiracy is not necessary to a Federal Trade Commission Act violation lacks specific meaning unless examined in the light of those cases in which it was developed.

Despite these weaknesses in the Federal Trade Commission's case against conscious parallelism of action, the sustaining of its arguments by both the circuit court of appeals and the Supreme Court would seem to be a vindication of its position. This conclusion is somewhat weakened, however, when we recall that the circuit court erroneously assumed that the issue to be decided in the *Conduit* case was identical with that decided in the *Cement* case, and that the Supreme Court did not hand down an opinion in the case because of the disqualification of one justice and the equal division of the others, but merely affirmed the circuit court's decision *per curiam*.

The force of the second count of the *Conduit* case is weakened even further by later statements of the Federal Trade Commission made under the pressure of a Congressional investigation. The Commission now seems willing to consider the second count of the *Conduit* case as simply a special remedy needed in this particular instance to secure effective relief from the conspiracy,[67] and appears ready to abandon

[64] "Under the Federal Trade Commission Act, where there is neither conscious parallel action which eliminates price competition nor monopolistic position maintained through unfair methods, a single enterprise is free to adopt any geographic pricing practice." FTC, STATEMENT OF POLICY, *supra* note 8.

[65] Federal Trade Comm'n v. Beech-Nut Packing Co., 257 U. S. 441 (1922).

[66] "The Sherman Act is not involved here except in so far as it shows a declaration of public policy to be considered in determining what are unfair methods of competition, which the Federal Trade Commission is empowered to condemn and suppress. . . . If the Beechnut system of merchandising is against public policy, because of 'its dangerous tendency unduly to hinder competition or to create monopoly,' it was within the power of the Commission to make an order forbidding its continuation." *Id.* at 453.

[67] *Hearings before Subcommittee of Senate Judiciary Committee on S. 1008*, 81st Cong., 1st Sess. 70 (1949).

its position on conscious parallelism of action as argued before the courts and espoused in its statement of policy.[68]

This seeming change in position by the Federal Trade Commission will not make the practice of basing point pricing any safer, however, as the Commission can, and undoubtedly will, continue to attack the system under the Federal Trade Commission Act by proving collusion in its adoption or use, or by showing that it is used to implement an agreement on prices. As was pointed out above, an analysis of the operation itself generally provides evidence that will be accepted by the Commission and the courts as sufficient to sustain a finding of collusion in the adoption or maintenance of the system. If the system cannot operate without these tell-tale signs of conspiracy, the Commission can successfully proceed against its common and collective use without resort to the conscious parallelism of action theory.

The most recent basing point case to reach the courts demonstrates very well the Commission's ability to proceed successfully against such a use of the system as being a conspiracy in restraint of trade. In *Bond Crown & Cork Co. v. Federal Trade Commission*,[69] the respondent manufacturers of bottle crowns and their trade association, the Crown Manufacturers Association of America, petitioned to have reviewed and set aside an order of the Federal Trade Commission finding that they were engaged in a conspiracy and combination in restraint of trade which was an unfair method of competition in violation of the Federal Trade Commission Act.

The evidence which the Commission held supported such a finding and order was (1) the use of a freight equalization system resulting in identical prices of all sellers at any given delivery point, (2) rigidity in the price of crowns since 1938, (3) standardization of crowns through the Association, (4) adherence to the terms of a standard sales contract which was discussed before the Association in 1920 but never formally adopted, (5) patent license agreements between the largest manufacturer in the industry and other manufacturers, which contained a minimum price clause until shortly before institution of the proceedings by the Commission, and (6) the furnishing of price information to these licensees by the licensor.

The circuit court in affirming the Commission's order paid great deference to the "expertness" of the Commission and its power to infer conspiracy from such circumstantial evidence. The court seemed particularly impressed by the evidence as to price uniformity and rigidity, and that as to standardization of product.[70]

[68] See notes 59, 60, and 61 *supra*.

[69] 176 F. 2d 974 (C. C. A. 4th 1949).

[70] "We conclude the discussion on the sufficiency of the evidence by adverting again to the indisputable fact that through the business practices followed by petitioners it has resulted that in an industry of which they control 85 per cent there has been no price change in ten years and absolutely no price competition whatever. The product has been so standardized that there is no choice of any sort between the products of different producers, and a purchaser anywhere in the country can purchase at the same price including freight from any producer. It is argued that all this is the result of the free play of economic forces, but the Commission did not think so; and this is just the sort of question that Congress intended the Commission to decide." *Id.* at 981.

In this case the evidence introduced in addition to that as to the bare existence of the delivered price system was less than in any prior case. Both the Commission and the court placed great emphasis upon inherent features of the system itself. It is submitted that it is virtually impossible for several members of an industry to employ a basing point system of pricing without leaving a trail of evidence such as was accepted by the Commission and the courts in this case, and to a lesser extent in prior cases, as sufficient to prove an unlawful conspiracy in restraint of trade.

The Federal Trade Commission also has proceeded against the zone system where it is used as a price fixing device. In most of these proceedings there was no petition for court review. Between 1936 and 1938 the Commission proceeded against conspiracies to fix prices by means of zone systems in seven cases involving as many industries.[71] In each of these cases the allegations of the complaint were admitted or the facts were stipulated and a consent decree entered.

The first of such orders to be contested before the Commission and on review was *Scientific Apparatus Makers of America*.[72] It was found by the Commission that the zone system had been adopted pursuant to agreement and that there was an agreement to follow a price list that was circulated among the respondent blue print paper producers. These findings were upheld by the court of appeals on review.[73] The most important aspect of the case was that concerning the liability of two of the producers who had not joined in the original conspiracy, but who later followed the price system set up by the conspirators. As to them the court held:[74]

> One may be liable regardless of when he joins the unlawful trade practices. . . . We do not think that affirmative, positive express agreement to maintain prices is essential to establish unfair trade practices. If the parties clearly and intentionally maintain the prices, even though without express agreement they are liable. . . . An artificial price level not related to the supply and demand in a given commodity, may evidence concerted action of sellers operating to restrain commerce. That is what the evidence here shows.

The fact that actual agreement to adopt the system and fix the prices was shown had great influence upon the decision as to these two respondents; nevertheless, this case shows that the courts are willing to go a long way toward inferring concerted action from the mere use of a zone system. It of course also demonstrates that adherence to a system founded by agreement will be held illegal even though such adherence is not pursuant to agreement or combination.

[71] The Water Works Valve and Hydrant Group of the Valve and Fittings Institute, 24 F. T. C. 1253 (1937); Menasha Wooden Ware Corporation, 25 F. T. C. 57 (1937); United Fence Manufacturers Ass'n, 27 F. T. C. 377 (1938); Food Dish Associates of America, 27 F. T. C. 1267 (1938); Columbia Alkali Corporation, 27 F. T. C. 1354 (1938); Rowe Manufacturing Company, 27 F. T. C. 1376 (1938); Mathieson Alkali Works, Inc., 27 F. T. C. 1413 (1938).

[72] 33 F. T. C. 1130 (1941).

[73] Eugene Dietzgen Co. v. Federal Trade Comm'n, 142 F. 2d 321 (C. C. A. 7th 1944).

[74] *Id.* at 331, 332.

An early attempt to eliminate the need for proof of conspiracy in enforcing its orders against zone systems was made by the Commission in *Salt Producers Association v. Federal Trade Commission*.[75] The complaint ran against eighteen salt companies and the Salt Producers Association and charged a combination to monopolize and suppress competition in the sale of salt, to fix unfair prices, and to establish zones to aid in fixing of prices, etc. The respondents admitted the allegations of the complaint but objected to the terms of the order which ordered respondents to cease and desist from participating in "any common course of action, mutual agreement, combination or conspiracy, to fix or maintain the prices of salt" and from "establishing or maintaining delivered price zones, or making quotations and sales of salt upon a delivered price basis under a zone system whereby the cost of salt delivered to buyers within each respective zone is made identical at all destinations within such zone."[76]

The respondents objected strenuously to the inclusion of the phrase "common course of action" in the order, contending that it would include common action occurring through pure happenstance. The Commission, on the other hand, contended that it did not apply to independent action "undertaken independently without previous agreement therefor." The court reasoned that since the Commission intended only to accomplish the prohibition of planned mutual action it would be fair to add "planned" before the disputed phrase.

The respondents also objected to the order's prohibition of the establishment of uniform prices for specified zone areas and asked that individual sellers be allowed to utilize the zone method of pricing. The court remarked that it was the Commission's aim only to eliminate all concert of action, and that the complaint did not show an attack upon the zone system per se as an unfair method of competition by one manufacturer in relation to two of his customers, and concluded that the respondents should not be denied all right to use of the zone method of pricing.

It seems that here the Commission was attempting to accomplish with respect to zone systems what it accomplished with respect to the basing point system in the second count of the *Conduit* case. It failed because its complaint was directed solely at combination or conspiracy, and because it made no determination of the unfairness of the system when used by one manufacturer in such a situation. In the *Conduit* case the Commission remedied both of these deficiencies by alleging that knowing parallel use of the basing point system was an unfair method of competition, and that the individual manufacturer in such circumstances discriminated against his nearby purchasers.

The principle of the second count of the *Conduit* case is undoubtedly equally applicable to the parallel use of the zone system by a number of sellers.

[75] 134 F. 2d 354 (C. C. A. 7th 1943).
[76] 34 F. T. C. 38 (1941).

The zone system case which has prompted the most discussion and controversy is *Fort Howard Paper Co. v. Federal Trade Commission*.[77] Involved were a trade association, and eight corporations who were members, or had been members, of the trade association, and who comprised all the manufacturers of crepe paper in the United States. The respondents were charged with being engaged in a "conspiracy, combination, agreement, and understanding for the purpose and with the effect of restricting, restraining, suppressing and eliminating price competition among respondent manufacturers in the sale of crepe paper in commerce. . . ."[78]

There was some evidence of a price fixing agreement under the N.I.R.A. and of its continuation after the N.I.R.A. was invalidated. The bulk of the evidence, however, consisted of a showing of the existence and use of the zone pricing system and the cooperative trade practices, such as classification of customers, uniform product standards, and filing of price lists with the association, which were followed in order to facilitate and maintain the system. From this evidence the Commission found that the zone system was cooperatively adopted and maintained and hence was the device used to set up and maintain uniform prices for the sale of crepe paper.

The court upheld the Commission's findings and, as in the *Milk Can* case, placed much more emphasis upon the significance of the identical delivered prices than did the Commission,[79] and glossed over the many trade practices upon which the Commission relied to prove conspiracy.[80] The court by its opinion intimates that it would uphold an inference of conspiracy drawn from the bare industry-wide use of the zone pricing system.[81]

Although there has never been an attack upon the legality of a zone pricing system per se, in view of these recent cases it now seems quite likely that where it is used by a number of sellers in a given industry so that the customer is faced with identical delivered prices at all points, it will be unable to withstand an inference of conspiracy, except perhaps in the few instances in which the identity of prices may be explainable by the nature of the market, the type of product, or the transportation costs.[82] The recent tendency of the courts to emphasize and give great weight to the "expertness" of the Federal Trade Commission, as exemplified in the *Crown* case, greatly reenforces this conclusion. And, as pointed out with respect to the basing point system, the apparent abandonment of the conscious parallelism

[77] 156 F. 2d 899 (C. C. A. 7th 1946).

[78] 38 F. T. C. 282, 283 (1944).

[79] See note 35 *supra*. See also, Allied Paper Mills v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *cert. denied*, 336 U. S. 918 (1949).

[80] "We think the artificiality and arbitrariness of the zone structure is so apparent it cannot withstand the inference of agreement. The Commission evidently could not believe that Wisconsin companies would deprive themselves of the natural benefit of location in the midwest, and proximity to the west, over eastern competitors, were it not agreed that they would have equal chance for the eastern business, where most of the crepe paper manufacturers were located. 156 F. 2d 899, 907 (C. C. A. 7th 1946).

[81] See Wooden, *The Defense of Delivered Price Systems*, 15 GEO. WASH. L. REV. 1, 27 (1946).

[82] "When a group of competing sellers have all chosen to establish an unnatural zone system with identical boundaries and identical price differentials, it is difficult to believe that this result could be achieved and maintained without collusion." FTC, STATEMENT OF POLICY, *supra* note 8.

of action theory by the Commission will not render the Commission any less capable of successfully proceeding against the common or parallel use of a zone system on the ground of collusion in its adoption or use.

Although the Commission has never proceeded against the one zone price system, its proceedings against the multiple zone system indicate that where the prices of a number of sellers following such system are identical to such a degree that there is reflected the absence of an independent and individual determination to adopt them, this system will likewise be unable to withstand an inference of collusion and will be held illegal as an unfair method of competition under Section 5 of the Federal Trade Commission Act.

To the extent that the individual adoption and use of the one zone system is predicated upon a sincere desire to sell competitively in a nationwide market, the system will be immune from attack under the Federal Trade Commission Act. Consequently, the seller who wishes to use a one zone pricing system in order to exploit a nationally advertised brand may do so without fear of prosecution under the Federal Trade Commission Act if his price is independently determined. The frequently expressed fear that the Commission will mistake independently arrived at prices for conspiracy prices and succeed in convincing the courts of the validity of such findings seems unfounded.

These cases under the Federal Trade Commission Act are all based upon concerted or collective use of the delivered pricing systems and have little, if any, application to the problems arising from the individual and independent use of such systems.[83] Proceedings against individual and independent use of any of the delivered pricing systems have been had only under the Clayton Act as amended by the Robinson-Patman Act, and the number of such proceedings under that Act is very small.

IV

THE CLAYTON ACT AS AMENDED BY THE ROBINSON-PATMAN ACT OF 1936

The price discrimination elements in delivered price systems expose them to findings of illegality under the Clayton Act as amended by the Robinson-Patman Act. It is this aspect of the delivered price problem that has resulted in the most confusion and in the most controversy over the legality of the various systems.

This confusion and controversy may result from the attempt to apply a somewhat vague and poorly drafted statute to a variety of exceedingly complex business situations involving economic aspects which are little understood. It may reflect the natural reluctance of businessmen to give up a way of doing business that not only has proved lucrative, but also has helped to relax some of the rigors of competition which, although perhaps necessary to the preservation of the free enterprise system, have been to businessmen an evil to be avoided if possible. Perhaps it is a reflection of the unwillingness of some of the dominant figures of our

[83] See note 64 *supra*.

economy to give up some of the means which they have used to inflict their wishes upon their weaker competitors so as to enhance and perpetuate their own power and control. These and many other assertions are made in any discussion of the problem, and an economic theory can be found to fit every argument pro and con on this subject.

My purpose here is not to reconcile these economic arguments nor to criticize the Robinson-Patman Act or its enforcement by the Federal Trade Commission, but to set forth the present legal status of delivered price systems under the Act. Since the cases are not numerous, much emphasis is given to policy statements of the Federal Trade Commission, and there is of necessity much reference to material in the decided cases which admittedly is dictum.

The purpose of the Robinson-Patman Act was to amend Section 2 of the Clayton Act, which prohibited price discriminations in interstate commerce whose effect "may be to substantially lessen competition or tend to create a monopoly in any line of commerce." Although the Clayton Act was passed in 1914, it was not until 1930 that it was definitely decided that the Act applied to competition among the customers of the seller as well as to competition between the seller and his competitors.[84] Until that time the Act had been given a narrow construction to include only competition between the seller and his own competitors.[85]

One of the principal criticisms of the original Clayton Act was that it was too restrictive in requiring a showing of injury to general competitive conditions in the affected line of commerce, while the more important problem should be the injury to the competition of the person upon whom the discrimination was practiced.[86]

The Robinson-Patman Act was designed to eliminate this "weakness." So Section 2(a) of the new Act carried over the basic provisions of Section 2 of the Clayton Act with the added provision as to injury of competition with the individual seller or his customers and the customers of such customers. The basic provisions of the Clayton Act were not changed, and the Congressional intent seems to have been to continue the interpretation given to them under the original Act.[87] Section 2(a) provides in part:

> That it shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchasers involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the United States or any territory thereof or the Dis-

[84] George Van Camp and Sons Co. v. American Can Co., 278 U. S. 245 (1930).

[85] Mennen and Co. v. Federal Trade Comm'n, 288 Fed. 774 (C. C. A. 2d 1923).

[86] H. R. REP. No. 2287, 74th Cong., 2d Sess. 8 (1936); American Can Co. v. Ladoga Canning Co., 44 F. 2d 763, 766 (C. C. A. 7th 1930), *cert. denied*, 282 U. S. 899 (1931).

[87] Representative Utterback stated that these provisions "correspond to those required to be shown under the old Section 2 of the Clayton Act. Generally speaking they require a showing of effect upon *competitive* conditions generally in the line of commerce and market territory concerned as distinguished from the effect of discrimination upon immediate competition with the grantor or grantee." 80 CONG. REC. 9417 (1936).

trict of Columbia or any insular possession or other place under the jurisdiction of the United States and where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of them: Provided, That nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered.

No question can arise under this section of the statute unless there is a discrimination in price. The statute nowhere defines what is meant by discrimination, although it implies at least a difference in price.[88] It is important to note also that this discrimination or difference is not unlawful unless its effect "may be" that which is set out in the statute.

Since a difference in price is essential to illegal action under the statute, it becomes important to know how this difference is to be determined. This is particularly important when the application of the Act to delivered price systems is considered. There are two ways in which the difference in price may be determined. One method is to deduct all freight costs from the amount paid by the buyer and examine the net amounts realized at the plant.[89] If this method is used all forms of delivered pricing except f.o.b. mill pricing without freight equalization must create differences if sales are made at more than one point. Another method is to examine the delivered prices of buyers in different localities. If this method is used differences must exist in all cases of delivered prices except where a one zone system is used. It thus becomes apparent that if only the delivered prices are examined the one zone system cannot violate the Act as it involves no difference in price upon which to base a charge of discrimination.

[88] Representative Utterback, Chairman of the House Managers on the Robinson-Patman Act, in explaining this bill to Congress, had this to say about the meaning of discrimination: "In its meaning in simple English, a discrimination is more than a difference. Underlying the meaning of the word is the idea that some relationship exists between the parties to the discrimination which entitles them to equal treatment, whereby the difference granted to one casts some burden or disadvantage upon the other. If the two are competing in the resale of goods concerned that relation exists." 80 CONG. REC. 9416 (1936).

This definition is concerned only with competition in the second line, although the Act speaks of competition in the primary and in the third line. Consequently, we should add to the definition that a difference is discriminatory also which occurs where there are competitive conditions existing between the seller and his competitors and between customers of the purchasers from the seller, or between the customers of the competitors of such purchasers. Actually about all we can say in the way of definition is that for there to be a discrimination there must be a difference in price, but not all differences are necessarily discriminatory.

[89] The Federal Trade Commission sponsored an amendment to the Robinson-Patman Act which provided: "The word price, as used in this Section 2, shall be construed to mean the amount received by the vendor for each commodity unit, after deducting actual freight or cost of other transportation, if any, allowed or defrayed by the vendor." H. R. REP. No. 8442, 74th Cong., 2d Sess. (1936).

The definition was eliminated from the final bill. Representative Citron, of the House Judiciary Committee, stated that it should be dropped because "serious consequences of the inclusion of this definition of price . . . would be to compel all manufacturers to ship f.o.b. shipping point." 80 CONG. REC. 8224 (1936).

During the same session Congress considered, but failed to enact, the Wheeler Anti-Basing Point Bill. 80 CONG. REC. 8102, 8223 (1936).

The legality of the one zone system may depend then upon which conception of price prevails. The adoption of the "mill net" theory also may expose the uniform delivered prices within the zones of the multiple zone system to findings of discrimination. Basing point, freight equalization, and multiple zone price systems all produce differences in price which may be illegal regardless of which conception is followed.

It has been contended that since a difference in delivery cost does not necessarily result from the different methods or quantities in which the commodities are sold or delivered a difference in price cannot be justified by a showing of difference in delivery cost.[90] This argument appears valid if judged from a strict grammatical viewpoint. However, the intent of the framers of the Act seems contrary. Representative Utterback, Chairman of the House Managers, in explaining the bill stated:[91]

> Where the methods of delivery are the same, but the distance is different, price differences in such cases may, of course, be made to reflect those differences.

Moreover, the Federal Trade Commission and the courts have always assumed that such differences may be so justified. This proviso constitutes an affirmative defense to a charge that a price differential is an unlawful discrimination under the Act. It follows that any price difference which does not reflect differences in cost stands unexcused under this proviso and the Commission has taken the position, likewise accepted by the courts, that if it has the effect upon competition contemplated by the statute it is unlawful unless it can be justified under some other provision of the Act.[92]

A further provision of the Act pertinent to our discussion is Section 2(b),[93] which has given rise to much doubt as to whether the Federal Trade Commission has the burden of showing that a price discrimination has the requisite statutory effect on competition, or whether this burden rests upon the respondent once a difference in price, under circumstances making such difference a discrimination, has been shown. There is also doubt as to whether this section makes the good faith meeting of an equally low price of a competitor a substantive defense.

The use in this section of the terms "prima facie" case and "rebuttal" is largely responsible for the confusion and controversy which exist. On its face the section would seem to authorize the Commission to issue a cease and desist order when it finds that a price discrimination has been practiced. It seems, however, that the

[90] Hilder, *The Attack Upon Delivered Price Systems*, 14 GEO. WASH. L. R. 397, 414 (1946).

[91] 80 CONG. REC. 9417 (1936).

[92] See Wooden, *supra* note 81, at 14.

[93] "Upon proof being made, at any hearing on a complaint under this section that there has been discrimination in price or services or facilities furnished, the burden of rebutting the prima facie case thus made out by showing justification shall be upon the person charged with a violation of this section, and unless justification shall be affirmatively shown, the Commission is authorized to issue an order terminating the discrimination: Provided, however, that nothing herein contained shall prevent a seller rebutting the prima facie case thus made by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor."

Commission in its early proceedings under the Act never claimed such authority. It always followed its proof of discrimination with proof of the requisite effect on competition.[94] Then in 1945 in the *Moss* case,[95] the Court of Appeals for the Second Circuit raised serious doubts as to the necessity of the Commission's proving the effect upon competition.

In this case the Commission's complaint alleged that the respondent's price discriminations had produced the proscribed effect on competition and the Commission made findings adequate to support this allegation.[96] Despite this pleading of effect on competition and the affirmative finding directly on that point, the court in reviewing the case stated:[97]

> The Commission's position was that, having proved this (price discrimination), Section 2(b) put upon the petitioner the burden of justifying the discrimination, and warranted the order if it failed to do so.

The court then said that it was the Commission's burden to prove a difference in price and that there were competitors who might have been able to meet the higher price but could not meet the lower one. It then pointed out that the burden of proving the harmful effect on competition was difficult:[98]

> Hence Congress adopted the common device in such cases of shifting the burden of proof to anyone who sets two prices and who possibly knows why he has done so, and what has been the result. If he can prove that the lower price did not prevent or tend to prevent anyone from taking away the business he will succeed, for the accuser will not have brought him within the statute at all. Nevertheless he may succeed even though he fails to establish such a negative; for although it will then appear that he has lessened, or prevented, competition, the proviso of Section 2(b) will still excuse him, if he can show that his lower price did not undercut his competitors, but merely met their "equally low price." In short that is a defense to the violation of Section 2(a). This is as we interpret Section 2(a) and Section 2(b), when read together.

Thus, we have this court enunciating the rule that the accused has the burden of proving that his discrimination did not affect competition in the manner prohibited by the statute. This, despite the history of the Commission's prior practice and the fact that the Commission actually pleaded and found the proscribed effect on competition in this case.

The Commission was not long in taking advantage of this court's interpretation of the burden of proof, and in attempting to disprove that Section 2(b) provided a substantive defense to a price discrimination which had the proscribed effect upon competition. In October of that same year, 1945, the Commission filed its com-

[94] See Haslett, *Price Discriminations and Their Justification Under the Robinson Patman Act of 1936*, 46 MICH. L. REV. 450, 474 (1948).

[95] Samuel H. Moss, Inc. v. Federal Trade Comm'n, 148 F. 2d 378 (C. C. A. 2d 1945), *cert. denied*, 326 U. S. 734 (1945).

[96] 36 F. T. C. 640, 649 (1943).

[97] 148 F. 2d 378, 379 (C. C. A. 2d 1945).

[98] *Ibid.*

plaint, findings, and order in the *Standard Oil Co.* case.[99] In this case the Commission alleged and made affirmative findings that the respondent sold gasoline to different customers at different prices and that this constituted discriminations in price whose effect "has been and may be to injure, destroy and prevent competition" with the named respondents and "with their respective customers, in the resale of gasoline."

The respondent offered evidence that its lower prices were made to meet the equally low price of competitors but the Commission refused to receive this evidence contending that, even if the lower prices were so made, "This does not constitute a defense in the face of affirmative proof that the effect of the discrimination was to injure, destroy, and prevent competition."[100]

The Commission's theory of the Section 2(b) defense was set out at great length. Its contention was that a prima facie case was made out by proving (1) jurisdiction, (2) goods of like grade and quality, and (3) discrimination in price. This prima facie case may be rebutted if the respondent can show that his lower price was made in good faith to meet an equally low price of a competitor. This is declared to be not a substantive defense, however, and if the Commission can then show that "the effect of the discrimination may be to substantially lessen competition or tend to create a monopoly or to injure, destroy, or prevent competition between respondent and its competitors or between customers of the respondent or with the customers of such customers,"[101] it has proved an illegal discrimination.

The Commission appears to accept the rule of the *Moss* case as to the burden of proof and reject it as to the nature of the defense under Section 2(b).

This construction of Section 2(b) certainly places a heavy burden upon the respondent, and it has led to charges that the Commission and the courts have substituted the presumption of guilt for the traditional presumption of innocence in the enforcement of the Act.[102]

If this construction of Section 2(b) is accepted by the courts, the only substantive defense to a charge of unlawful price discrimination will be the "due allowance" proviso, and if this fails the Commission in many cases will not even have to show the proscribed injury to competition. The importance of this to the question of the legality of delivered pricing systems becomes apparent when it is recalled that all of these systems, except perhaps the one zone system, produce price differences which cannot be justified by this "due allowance" proviso.

[99] Standard Oil Co., 41 F. T. C. 263 (1946).

[100] *Id.* at 282.

[101] *Id.* at 283.

[102] "It seems to me that the trend of both administrative and judicial opinion relating to the Robinson-Patman Act . . . has been toward substituting the ancient presumption of innocence for one of guilt, toward a shifting of the burden of proof from the prosecution to the defense. In the case of the Robinson-Patman Act, this trend is evidenced by the practical elimination of the necessity for the prosecution to establish the injurious competitive effect of an allegedly discriminatory pricing policy and by sweeping away the defenses and justifications originally contained in the act." Allen C. Phelps, *Hearings*, *supra* note 13, at 135.

It is certainly not clear from a study of the terms of the Act and its legislative history that this is not what Congress had in mind when it passed the Act. Certainly the overriding purpose of the Act was to secure equality of price between buyers, whether they be large or small.[103] In both houses of Congress Section 2(b) was described as merely a rule of evidence rather than a part of substantive law.[104] The United States Court of Appeals for the Seventh Circuit upheld the Commission's order and approved its construction of Section 2(b).[105] However, it seems unlikely that the Supreme Court would have given so much attention to this defense in the delivered pricing cases if it had considered it as merely a rule of evidence. It is difficult, therefore, to predict the way in which the Court will hold on this issue. In view of the legislative history of the Act, it is quite probable that the Court will affirm the decision of the circuit court despite its rather obvious adherence to a contrary construction in the prior cases.

There are no decided cases involving delivered price systems under Section 2 of the old Clayton Act. An important Commission proceeding under this section was the *Pittsburgh Plus* case, mentioned previously. There the Commission alleged that there were discriminations in price the effect of which was to lessen competition betwen the favored customers of defendant and those discriminated against, and to lessen competition among all the producers of steel. The effect upon competition in the second line was proved by showing the much higher delivered prices charged to buyers west of Pittsburgh as compared with prices charged eastern buyers close to the single basing point, and the resultant inability of these western buyers to compete with the favored eastern buyers. Although it was the delivered price that was alleged to be discriminatory, the Commission in its findings spoke of the difference in mill nets as a measure of the discrimination, and found that the use of the single basing point system deprived purchasers located close to the production point of an advantage in the delivered price which they should have enjoyed over customers of the same seller located farther from the mill.

The injury to competition in the primary line was found in the fact that all steel producers followed the system, thereby producing a condition of matched prices and elimination of price competition among competing sellers.

In 1948 the respondents in the *Pittsburgh Plus* case narrowed the issue by their petition for review of the question of whether the order forbade the practice of systematically adopting competitors' base prices plus the freight from competitors' places of manufacture and shipment; *i.e.*, whether it forbade freight absorption

[103] See Crowley, *Equal Price Treatment Under the Robinson-Patman Act*, 95 U. OF PA. L. REV. 306, 343 (1946); see also 80 CONG. REC. 8102-8104 (1936).

[104] "It is to be noted, however, that this does not set up the meeting of competition as an absolute bar to a charge of discrimination under the bill. It merely permits it to be shown in evidence. This provision is entirely procedural. It does not determine substantive rights, liabilities, and duties." Representative Utterback, 80 CONG. REC. 9418 (1936).

"The proviso [Sec. 2(b)] to which he refers is simply a rule of evidence rather than a part of substantive law." Senator Van Nuys, 80 CONG. REC. 9903 (1936).

[105] Standard Oil Co. v. Federal Trade Comm'n, 173 F. 2d 210 (C. C. A. 7th 1949).

when not accompanied by phantom freight. They contended that this was really only the question whether they should be allowed to meet competition in good faith.

The Commission in its brief on this point contended that freight absorption was present and considered in the case; that freight absorption was so woven into the basing point system that it was not possible to prevent the one and permit the other; that the petitioners' practice of systematic freight absorption involved unlawful price discriminations under the Clayton Act, Section 2; that it did not constitute a good faith effort to meet competition "because it is part of a system by which petitioners and their competitors are enabled to match each others' delivered prices and neutralize the competitive effect of all cost differences; that it is not the meeting of individual competitive situations, and that like phantom freight it may injure competition among petitioners' customers."[106] It is important to note here that it was contended by the Commission that the injury to competition in the second line was caused not only by the higher delivered prices imposed as a result of the phantom freight, but also by the fact that because of freight absorption the buyers located next to the western mill paid a higher net price, thus placing them at a competitive disadvantage with eastern buyers paying a lower net price. This is a corollary to the Commission's arguments that the mill net is the true price and that the nearer buyer is entitled to a lower delivered price than those more distant from the plant. As will be brought out later, the upholding of this type of argument to prove injury to competition in the second line would make individual and independent use of any of these delivered price systems illegal under the amended Clayton Act. The extent to which this concept of injury to competition is accepted by the courts and utilized by the Commission will determine the legal fate of the individual, independent use of the one zone price system.

In the *Corn Products* case[107] the individual use of a single basing point system was attacked as producing discriminations in price in violation of the amended Clayton Act. In that case the Commission found that the respondent used Chicago as a basing point for all his delivered price quotations although he had plants both at Chicago and Kansas City. The Commission also found that in his use of the system he discriminated in price between his customers with the result that substantial injury was done to his competitors, competition with respondent tended to be hindered, suppressed and obstructed, it tended to create a monopoly in respondent, and substantial injury to competition among purchasers of such product was effected because of the lower prices granted to preferred purchasers and not to others.

The Commission based its finding of discrimination in price upon the fact that there were differences in prices to purchasers located in twelve different cities which differences could not be justified by the "due allowance" proviso. It found that purchasers located closer freightwise to Kansas City than Chicago paid a price

[106] Brief for Appellees, United States Steel Corp. v. Federal Trade Comm'n, Docket No. 6796 (C. C. A. 3d 1938).

[107] Corn Products Refining Co. v. Federal Trade Comm'n, 324 U. S. 726 (1945).

which included freight costs not actually incurred. Although no mention was made in the findings of the mill net, the findings indicated that the Commission's position was that there was a discrimination whenever the delivered price did not include the true transportation costs. If this be true, then, of course, the mill net would have to be examined to determine if the delivered price included freight costs different from those actually incurred.

The finding as to the adverse effects on competition was based upon the fact that purchasers from respondent were competitors in the sale of candy in which glucose was a principal ingredient. It was found that a difference of a fraction of a cent in the price of this candy would be sufficient to attract customers from one competitor to another. Consequently, it was concluded that the buyers paying the higher prices were injured in their efforts to compete with those who received the lower prices. It was found further that several candy makers located near Kansas City were forced to relocate by moving closer to Chicago in order to compete effectively.

The Supreme Court, in reviewing the decision of the circuit court[108] which upheld the Commission's order, noted the Commission's findings as to price differences in the twelve representative cities and pointed out that the net return at the Kansas City plant varied according to the phantom freight included in the delivered price. It referred to the Commission's findings that buyers in cities other than Chicago paid higher prices which resulted in higher costs of producing candy and in a lessening of these buyers' ability to compete with buyers in Chicago. In answer to the petitioners' argument that their pricing system did not result in price discriminations within the meaning of the Robinson-Patman Act the Court said:[109]

> Petitioners' pricing system results inevitably in systematic price discriminations, since the prices they receive upon deliveries from Kansas City bear relation to factors other than actual costs of production or delivery.

It then called attention to the varying net prices received by the petitioners from sales in the selected twelve cities and to the phantom freight collected from these sales and concluded:[110]

> The price discriminations resulting from this systematic inclusion of the freight differential in computing the delivered price are not specifically permitted by the statute. Hence they are unlawful, unless as petitioners argue, there is an implicit exception to the statute for such a basing point system.

This is a direct approval of the Commission's finding that delivered prices which fail to make due allowance for differences in the cost of delivery are discriminatory. The variations in mill net here were taken as proof that due allowance had not

[108] 144 F. 2d 211 (C. C. A. 7th 1944).
[109] 324 U. S. 726, 732 (1945).
[110] *Id.* at 733.

been made. In another part of the opinion the Court showed that it endorsed this concept of discrimination:[111]

> Further we have seen that prices in cities to which shipments are made from Kansas City are frequently discriminatory, since the prices in such cities usually vary according to factors, phantom freight or freight absorption, which are unrelated to any proper element of actual cost.

The Court next overruled the petitioners' contention[112] that the elimination from the Robinson-Patman Act of the definition of the word "price" as the mill net to the vendor showed a Congressional intention to sanction all basing point systems.[113]

In its examination of the findings as to the effect on competition of petitioners' discriminatory prices, the Court seemed to ignore the charge and findings of injury to competition in the primary line and considered only the injury to competition in the second line, that is, among customers of the petitioners. The Court sustained the Commission's finding of probable injury to competition based upon evidence that a small variation in the price of glucose was enough to divert business from one candy manufacturer to another, and upon evidence that some customers of the petitioners had actually been forced to relocate.

The competition which the Commission found probably would be injured by the use of the basing point system was that between respondent and his competitors (primary line), and that among the customers of the respondent (second line). The former injury is that which the discriminatory seller imposes upon his competitors by quoting lower prices to their customers so as to endanger their continued ability to compete with him, thus tending to give the seller a monopoly in the commodity sold. This concept of injury to competition is not a new one and is the one mainly responsible for the passage of the original Clayton Act. It is surprising that the Commission did not emphasize this concept of competitive injury, as its predatory nature would preclude its being defended as a "good faith" meeting of the "equally low price of a competitor."[114]

The *Staley* case[115] was a companion case to the *Corn Products* case. The respondent in that case had one plant at Decatur, Illinois, and sold all his products at delivered prices calculated by adding to a base price at Chicago the freight from Chicago to the buyer's destination. The Commission's complaint, findings, and order closely parallel those of the *Corn Products* case with the one exception that the only competitive injury alleged was that among the customers of the respondent.

[111] *Id.* at 739.

[112] See note 89 *supra*.

[113] "We think this legislative history indicates only that Congress was unwilling to require f.o.b. factory pricing, and thus to make all uniform delivered price systems and all basing point systems illegal per se. And to the contrary we think that it left the legality of such systems to be determined accordingly as they might be within the reach of Section 2(a) as enacted, and its more restricted prohibitions of discriminations in delivered prices." 324 U. S. 726, 737 (1945).

[114] For an interesting account of the predatory nature of basing point systems, see MACHLUP, *op. cit. supra* note 46, c. 5.

[115] Federal Trade Comm'n v. A. E. Staley Mfg. Co., 324 U. S. 746 (1945).

The Commission's order was vacated by the Court of Appeals for the Seventh Circuit. One majority judge believed that the respondent had rebutted the Commission's prima facie case by showing that he had adopted the basing point system in good faith to meet the equally low prices of his competitors. Another decided that the Commission had not made out a case of unlawful price discrimination. The third judge dissented and would have upheld the Commission's order. The Supreme Court in reviewing the case on certiorari reversed the decision of the lower court and upheld the Commission's finding that the respondent's pricing system involved price discriminations prohibited by Section 2(a) of the amended Clayton Act. As to these discriminations the Court had this to say:[116]

> As we hold in the Corn Products Refining Co. case with respect to a like system, price discriminations are necessarily involved where the price basing point is distant from the point of production. This is because, as in respondent's case, the delivered prices upon shipments from Decatur usually include an item of unearned or phantom freight or require the absorption of freight with the consequent variations in the seller's net factory prices. Since such freight differentials bear no relation to the actual cost of delivery, they are systematic discriminations prohibited by Section 2(b) whenever they have the defined effect upon competition.

The only question which the Court felt obliged to determine was whether the respondent had justified his discriminations under the "good faith" proviso of Section 2(b).

The respondent attempted to justify the discriminations by showing that he merely adopted the pricing system being utilized by his competitors when he entered the market. The Court rejected this argument, however, on the reasoning that he could not justify his discriminations by showing that he adopted the unlawful system of a competitor.

The Court recognized that the seller's adoption of a competitor's prices by including unearned freight in its delivered price was no different from maintaining an f.o.b. factory price high enough to take advantage, through freight absorption, of a competitor's higher price based on its higher cost of delivery, and that such action caused an artificially high price level. This was a recognition by the Court of the fallacy of seeing phantom freight as the only evil in the basing point system, and strongly indicates that a defense under Section 2(b) would not be any more available to sellers utilizing a freight equalization system involving only freight absorption.[117]

In rejecting the respondent's defense under Section 2(b) the Court also remarked:[118]

[116] *Id.* at 750, 751.

[117] "So far as injury to competition among the customers of a single seller is concerned, the discrimination reflected by the varying mill nets of freight absorption may hurt a customer just as much as an equal amount of discrimination taking the form of phantom freight." Wooden, *The Concept of Unlawful Discrimination as It Applies to Geographic Price Differences*, 37 GEO. L. J. 166, 180 (1949).

For a more sophisticated explanation of the fallacy of attempting to differentiate between the freight absorption and phantom freight involved in basing point systems, see MACHLUP, *op. cit. supra* note 46, at 149-151.

[118] 324 U. S. 746, 757 (1945).

> We cannot say that a seller acts in good faith when it chooses to adopt such a clearly discriminatory price system, at least where it has never attempted to set up a non-discriminatory pricing system, giving to purchasers, who have the natural advantage of proximity to its plant, the price advantages which they are entitled to expect over purchasers at a distance.

This indicated the Court's approval of the Commission's argument, made in the *Pittsburgh Plus* case and in several proceedings[119] involving collusive use of a delivered price system, that the purchasers located close to the plant have a natural right to a price advantage over those located a greater distance therefrom, and that any system not giving them that advantage is discriminatory.[120]

If delivered prices which do not make due allowance for differences in cost of delivery are discriminatory, and if the buyer located closer to the plant has a natural right to a delivered price advantage over more distant purchasers, it follows that in order to determine the presence and extent of discrimination in a delivered price the price without the transportation cost included, that is, the mill net price, must be examined. It is difficult to see how these two propositions could be accepted without accepting as the concept of price the mill net received by the vendor. There is dispute, however, as to whether these two cases represent approval of the "mill net" theory.[121] It is, of course, true that there were differences in the sellers' delivered prices in these cases which could not be justified under the "due allowance" proviso. Consequently, a decision on the "mill net" question was not necessary to a determination of either case. The many references of the Court to the mill net price cannot be overlooked, however, and the fact that the cases could have been

[119] American Chain Institute, Inc., Docket No. 4878 (1945); American Iron and Steel Institute, Docket No. 5508; Clay Sewer Pipe Ass'n, Docket No. 5484; National Lead Co., Docket No. 5253 (1944).

[120] One writer characterizes this argument as "a conclusion which lacks support" and says, "It is just as easy to argue that competition would be fostered if buyers were not penalized by location at a distance from the factory." Hilder, *supra* note 90, at 414, 415.

Another answers this contention: "Now it is obvious that unless buyers have that right then sellers have the right to charge buyers near the factory more than those at a distance. That involves charging them phantom freight or refusal to make due allowance for differences in cost of delivery. It may 'be just as easy' to contend that competition would be fostered if distant buyers were not penalized but it is not just as sound. Whatever penalty they are under it is one imposed by nature or by their own choice of location and not by fiat of the seller on nearby purchasers. That penalty is the act of a discriminator." Wooden, *supra* note 81, at 12.

[121] "Obviously if due allowance is made there will be no difference in the mill net or f.o.b. factory prices applying to the various destinations involved. To whatever extent due allowance is not made it will reflect itself in varying net prices and the amount of the variation would be the amount of the discrimination." Wooden, *supra* note 117, at 167.

"The Court evidently found the difference between the delivered prices on Corn Products' shipments from Kansas City to have no reasonable explanation, since these differences did not reflect differences in freight costs from Kansas City. To make this finding it was not necessary to consider mill net returns." Hilder, *supra* note 90, at 416.

"In each case the Supreme Court referred, in part, to the discriminatory 'mill nets' received by Corn Products and Staley in their use of basing points other than points of shipment, but affirmed the Commission's orders on the ground that there were differences in the delivered prices, which could not be justified by the sellers. The 'mill net' theory of price discrimination, thus, although frequently referred to has not been determinative in any of the cases decided so far." Haslett, *supra* note 94, at 460.

decided without a consideration of the seller's mill net does not definitely settle the question of whether they were so decided.

The Court further confused the issue of its acceptance of the "mill net" concept of price by adding, after its discussion of discrimination and rejection of the Section 2(b) defense:[122]

> But it does not follow that respondents may never absorb freight when their factory price plus actual freight is higher than their competitors' price, or that sellers, by so doing, may not maintain a uniform delivered price at all points of delivery, for in that case there is no discrimination in price.

Defenders of the one zone system have seized upon this statement as showing an express court sanction of such systems, and as express rejection of the "mill net" theory.[123] The chief proponent of the "mill net" theory, on the other hand, has described this statement of the Court as "a momentary aberration of thought," and mere "dictum."[124]

The statement certainly indicates that the Court gave little deliberative thought to the actual nature of a one zone system, because it violates the two propositions which the Court apparently accepted in holding the individual seller's use of the single basing point system illegal in these two cases. These are: (1) delivered prices which do not make due allowance for differences in delivery costs are discriminatory; and (2) the buyer close to the factory has a right to a delivered price advantage over buyers located a greater distance therefrom. Furthermore, the Court speaks of maintaining a uniform delivered price system by means of freight absorption when in fact such a system also inevitably contains an element of phantom freight in that the averaging of the freight costs among buyers results in the nearby buyer paying an imputed freight factor greater in amount than the actual freight of such buyer.

In a case involving directly the legality of a one zone system wherein the Commission would be certain to point out these aspects of the one zone system, the Court probably would not let this dictum prevent it from holding that the one zone system inevitably produces discriminatory prices.

These two cases indicate that in basing point cases where the injury to competition is on the buyer's side the defense of meeting a competitor's equally low price in good faith will have a very narrow scope of application, if indeed it can ever be successfully urged. It is clear that if there is an industry-wide use of the system, either the single, multiple or plenary type, this defense will fail. Likewise, where the seller uses a pricing formula under which he follows a discriminatory

[122] 324 U. S. 746, 757 (1945).

[123] "The Court could hardly have indicated more clearly its view that Section 2(a) has no application to the universal delivered price system." Hilder, *supra* note 90, at 415.

"Hence we must conclude that Section 2(a) does not reach a uniform delivered price, and in this event it is inherently valid thereunder." Dunn, *The Validity of a Uniform Delivered Price*, in CCH, ROBINSON-PATMAN ACT SYMPOSIUM BEFORE THE N. Y. STATE BAR ASS'N 13, 18 (1947).

[124] Wooden, *supra* note 81, at 19.

pricing policy even where there may be no competition to justify it, the defense will not succeed. This situation is apt to arise in any instance in which a delivered pricing system is rigidly adhered to. Where a multiple zone system is used in which the differences in price cannot be explained under the "due allowance" proviso of Section 2(a), it would seem that the arbitrary nature of the zone differentials in most instances would preclude any successful use of the Section 2(b) defense. As to the uniform prices within the zones of the multiple zone system and in the one zone system, the existence of phantom freight charges would preclude successful use of the defense.

It is important to note also that although neither of the concepts of injury to competition involved in these two cases depends upon conspiracy or conscious parallel action, there was a background of collusive use of the basing point system in this industry which further indicates that some sort of conspiracy or concerted action is essential to the effective functioning of a basing point system of pricing.[125]

The most recent delivered pricing case involving application of the amended Clayton Act to be decided by the Supreme Court was *Federal Trade Commission v. Cement Institute*,[126] the first count of which, alleging a combination to hinder and restrict competition, was discussed *supra*. The second count of the complaint in this case charged that this collusive use of the multiple basing point system of delivered prices constituted a combination to discriminate in price which resulted in discriminations in price in the sale of cement in violation of Section 2(a) of the amended Clayton Act. This count alleged that the delivered price was not the true price, and that "in order to derive the true price received, the price actually paid to the carrier for transportation of the cement to the buyer must be deducted from the delivered price."[127] It further alleged that the discriminations were made in order to destroy competition in price among the various sellers in violation of Section 2(a) of the amended Clayton Act, and that their effect was to destroy competition among all sellers granting the discriminations.

The Commission found that the systematic discrimination in mill nets was an inherent and necessary part of the multiple basing point system, which was itself an expression of each seller's effort to match the delivered prices of the other sellers. The use of the system to match prices and thereby avoid price competition was found to preclude any defense of the varying mill nets as being made in good faith to meet the equally low price of a competitor. The Commission concluded that the systematic discriminations in mill nets were discriminations in price unlawful under Section 2(a) of the amended Clayton Act, and that their effect "has been and may be substantially to lessen competition and tend to create a monopoly in the sale and distribution of cement, and has been and may be to injure, destroy

[125] See Sheehy, *The Legal and Factual Content of Recent Geographic Pricing Cases*, 37 GEO. L. J. 183, 200 (1949); see note 46 *supra*.

[126] 333 U. S. 683 (1948).

[127] 37 F. T. C. 87, 117 (1943).

and prevent competition with respondents who grant and exact such discriminations."[128]

The Court of Appeals for the Seventh Circuit reversed the Commission on Count II. It agreed that prices involving phantom freight were illegal, but held that those involving only freight absorption came within the good faith proviso of Section 2(b). This Court also, of course, failed to uphold the Commission's findings of conspiracy.[129]

The Supreme Court answered the respondents' contention that their varying net returns did not constitute discriminations under Section 2(a) by pointing to the decisions in the *Glucose* cases, and stated that "the combined effect of the two cases was to forbid the adoption for sales purposes of any basing point system."[130]

The defense of a good faith meeting of competition was disallowed by the Court on the grounds that Section 2(b) did not permit a seller to employ a pricing system "which constantly results in his getting more money for like goods from some customers than he does from others,"[131] and that all of respondents made some sales whose prices were determined by the basing point formula and governed by other base mills. This the Court said was proof of the use of the system as a practice rather than as a "good faith effort to meet *individual competitive situations*."[132]

So here we see the Court apparently accepting the Commission's theory that it is the difference in mill nets which measures the discrimination, and that the mill net must be taken as the true price. The Commission, of course, did introduce evidence tending to show that the respondents considered the mill net as the true price, but this does not seem sufficient to justify a conclusion that the Supreme Court did not accept the "mill net" concept of price.[133] Such a rationalization of the case seems even more weak when we recall the reference made to mill nets in the previous cases. In view of the *Corn Products*, *Staley*, and *Cement* cases it seems safe to assume that a finding of discrimination in price within the meaning of Section 2(a) of the amended Clayton Act will be upheld whenever there are differences in the mill nets from the sale of goods of like grade and quality, which do not come within the "due allowance" proviso of that section.

If this assumption is valid, and this test of discrimination is followed in cases dealing with the other delivered price systems, the freight equalization, multiple zone, and one zone price systems also must be held discriminatory, as differences in mill nets not justifiable under the "due allowance" proviso are inherent in and necessarily result from the use of each of these systems. Of course this does not neces-

[128] *Id.* at 257.

[129] 157 F. 2d 533 (C. C. A. 7th 1946).

[130] 333 U. S. 683, 723 (1948).

[131] *Id.* at 725.

[132] *Ibid.* (Italics supplied.)

[133] One writer contends that the *Cement* case cannot be cited as one in which the Court defined price as the mill net because of this special evidence introduced by the Commission. He says that "price" in Section 2(a) means "whatever the circumstances of the transaction make it." Sheehy, *supra* note 125, at 218.

sarily mean that they are unlawfully discriminatory, as the discriminations must have the effect on competition proscribed by the statute, and there is also the scant possibility of justification under Section 2(b).

The competitive injury found where the price discriminations are the result of concerted use of a basing point system is injury to competition in the primary line, which is not imposed by a single seller, but is the result of the cooperative setting aside of price competition through the deliberate matching of prices. The holding in this case is based upon the collusive maintenance of the basing point system,[134] but if it be admitted that a parallel or common use of a basing point system in which price discriminations are inherent results in the same matching of prices and setting aside of competition, the proving of conspiracy would seem not to be necessary to prove this injury to competition on the selling side of the market. The Commission recognized this in the *Pittsburgh Plus* case and found that the discriminations of a single seller using the basing point system were unlawful because they worked this injury to competition where the remaining sellers likewise followed the same system.

The Circuit Court of Appeals in the *Conduit* case, *supra*, accepted the proposition that a knowing and parallel use of the basing point system resulted in the individual seller practicing discrimination which had the same effect on competition as was found in this case to be the result of a conspiracy, and the Supreme Court upheld this acceptance of the proposition. True, the *Conduit* case was decided under the Federal Trade Commission Act and did not involve the Clayton Act, but its reasoning may compel a holding that the individual use of the basing point system with knowledge that others likewise use it, thereby resulting in identity of prices at all points, is unlawfully discriminatory under Section 2(a) of the Clayton Act regardless of any finding of conspiracy. The same reasoning will apply to any of the other delivered price systems which we have considered, if they are used in the same way so as to produce the same matching of prices at all points. Such a holding is not so startling as it at first might appear if it is but recalled that the injury to competition here is the same as would result from an unlawful conspiracy to maintain the system, and if we remember from our discussion under the Federal Trade Commission Act the very persuasive inferences of conspiracy which arise from such industry-wide use of these delivered price systems.

This case also further narrowed the scope of the area in which the "good faith" proviso of Section 2(b) might be available to a discriminating seller. Where the

[134] "As we read the order, all of its separate prohibiting paragraphs and sub-paragraphs, which need not here be set out, are modified and limited by a preamble. This preamble directs that all of the respondents 'do forthwith cease and desist from entering into, continuing, cooperating in, or carrying out any planned common course of action, understanding or agreement, combination or conspiracy, between and among any two or more of said respondents, or between any one or more of said respondents and others not parties hereto, to do or perform any of the following things. . . .' Then follow the prohibitory sentences. It is thus apparent that the order by its terms is directed solely at concerted, not individual, activity on the part of the respondents." 333 U. S. 683, 727, 728 (1948).

injury to competition is on the seller's side, and results from the cooperative matching of prices so as to eliminate competition, the defense is not available.

The Court also spoke in the *Staley* case of meeting individual competitive situations, and in both the *Corn Products* and *Cement* cases it spoke of systematic price discrimination as showing a lack of a good faith meeting of competition. It is not clear what the Court meant by these statements. Many have construed them to mean that the "good faith" proviso is inapplicable except in isolated transactions. Such a construction would, of course, make the "good faith" defense unavailable to a seller who individually and in an independent manner systematically, or as a business practice, absorbs freight to sell in a distant market in which he is at a disadvantage freightwise. I do not believe that these dicta can be stretched to cover such individual practices of freight absorption, but it certainly is a very strong indication that any seller who rigidly adheres to a delivered pricing system will be unable to defend his price discriminations successfully under Section 2(b).

As far as delivered price systems are concerned, then, the question raised in the *Standard Oil* case as to the nature of the Section 2(b) defense is of little importance. The question of who must bear the burden of proof as to injury to competition is still very important, however. Since the seller using a delivered price system cannot bring his discriminations within this section, the Commission, if its arguments as to burden of proof are upheld in the *Standard Oil* case, would in many cases have to show only the use of the discriminatory system in order to prove its case. In view of the past practice of the Commission and the almost insuperable burden that would otherwise fall upon the respondent, it is quite likely that the Commission will be held to have the burden of proving the injurious effect on competition in all cases even if the Section 2(b) defense is held to be not a substantive one. In view of the increasing pressure for amendment to the existing law, it would seem to be to the Commission's advantage to accept the burden voluntarily.

Since we have concluded that all these delivered price systems involve price discriminations, the important question becomes, what will be considered evidence sufficient to prove that these discriminations have the defined effect upon competition?

The pertinent words of the statute are "where the effect of such discriminations *may be* substantially to lessen competition," etc. The very wording of the statute indicates, and the cases have so held,[135] that an actual injury to competition need not be shown. The latest Supreme Court case to interpret this part of the Act was the *Morton Salt* case,[136] which did not involve delivered prices. In this case involving price discounts, the Court said:[137]

[135] Corn Products Refining Co. v. Federal Trade Comm'n, 324 U. S. 726 (1945); Federal Trade Comm'n v. Morton Salt Co., 334 U. S. 37 (1947).

[136] Federal Trade Comm'n v. Morton Salt Co., 334 U. S. 37 (1947).

[137] *Id.* at 46. The Court in the *Corn Products* case said ". . . The use of the word 'may' was not to prohibit discriminations having 'the mere possibility of those consequences,' but to reach those which would probably have the defined effect upon competition." 324 U. S. 726, 742 (1945). The Court took notice of this statement in the *Morton Salt* case but still concluded that the test was "reasonable possibility."

After a careful consideration of this provision of the Robinson-Patman Act, we have said that "the statute does not require that the discriminations must in fact have harmed competition, but only that there is a reasonable possibility that they 'may' have such an effect." Corn Products Co. v. F. T. C., 324 U. S. 726, 742.

A careful reading of the *Corn Products* case will reveal that the Court there did not actually use the test of "reasonable possibility." To say that the Court used the test of "reasonable probability" would probably be more accurate. It is doubtful if the Court in the *Morton Salt* case meant to depart from its prior interpretation of the statute, and even if it did do so the difference between "possibility" and "probability" may be in effect infinitesimal.[138]

The Court did suggest, however, that the required injury to competition could be inferred from substantial price differences without any other evidence as to their effect upon competition. The possibility of the Commission adopting such an approach in its delivered price proceedings has caused quite a furor. The Commission, however, has stated that it will not use the concept of injury adopted by the Court in the *Morton Salt* case. As to the test which it would follow the Commission said:[139]

The minimum determination of injury should be based upon ascertained facts that afford substantial probability that the discriminations if continued, will result in injury to competition. . . . The concept of injury applied in this field must be appropriate to the particular problem and not based merely upon analogy to concepts elsewhere. In basing point cases the Commission will continue to employ concepts of injury similar to those which it has used in the past.

If the Commission is to follow this statement it is important to determine what are "ascertained facts that afford substantial probability that the discrimination if continued, will result in injury to competition," and what are the "concepts of injury" which the Commission has used in the past.

[138] The following question was asked several witnesses in the course of the Hearings pursuant to S. Res. 241: "Does the law as interpreted by the Court permit the Commission to hold such a practice illegal if it finds a reasonable possibility of injury to competition?" These answers were received: "I think that was definitely determined in the *Morton Salt* case." Allen C. Phelps, Chief, Division of Export Trade, Federal Trade Comm'n, *Hearings, supra* note *13*, at 127. "My answer to that as it stands is 'NO,' because I believe there has been a great deal of exaggeration and unfounded assumption created and built upon the literal interpretation of those two words, 'reasonable possibility.' I believe that even the minority in the *Morton Salt* case did not properly take account of the context in which these two words were used." W. B. Wooden, Associate General Counsel, Federal Trade Comm'n, *id.* at 729, 730. "Section 2(a) makes a price discrimination unlawful where its effect may be substantially to lessen competition or to injure, destroy, or prevent competition. F. T. C. v. Morton Salt Co. held that a price discrimination comes within the ban of Section 2 if there is 'reasonable possibility' that it will have the defined effect upon competition.

"Prior to this decision it had not been definitely determined whether this section dealt with effect in terms of reasonable 'probability' or reasonable 'possibility.'

"I think it is clear that the Supreme Court has now adopted the latter view; but because of the connotations of the word 'reasonable,' I doubt that the difference between the two interpretations is, as a practical matter, very great." H. A. Bergson, Ass't Attorney General, Antitrust Division, Department of Justice, *id.* at 1381.

[139] FTC, STATEMENT OF POLICY, *supra* note 8.

The *Pittsburgh Plus* and the *Glucose* cases are the only delivered price cases in which an injury to competition among purchasers from the discriminating sellers was involved. In each case the injury to competition was found in the fact that the buyers discriminated against had constantly paid higher prices for their raw materials and thus could not effectively compete with the favored purchasers. It was shown also in each case that some customers were forced to relocate their businesses in order to continue to compete with the favored purchasers. It is also significant that in each case the buyers paying significantly different prices were in actual competition with each other.

If this concept of injury to competition is followed, an injury to competition among customers is quite likely to be found in any case where a single seller uses a single or multiple basing point system and his customers are in competition with one another, or where a single seller uses a multiple zone system with buyers along the fringes of the zones in competition and paying significantly different prices because of the differentials between zones; the price differentials not being justifiable under the "due allowance" proviso. The possibility of such injury flowing from the single seller's use of the freight equalization system is rather remote as the buyers paying significantly different prices are more apt to be located in different market areas and hence not in competition in resale of the product. Of course, as was seen in the *Glucose* cases, the competition among purchasers does not have to be in resale of the commodity purchased but may be in the sale of a product manufactured therefrom. The type of the commodity sold under the various systems might be important, therefore, as the probability of competition among purchasers will vary with the commodity. The type of commodity so sold may likewise be important in that the price difference must be great enough so that it may lessen competition substantially. This means that if the product is one for which the freight charge is a relatively important factor there is apt to be a price difference great enough to cause the prohibited effect upon competition, whereas with respect to many products the freight charge is a relatively small fraction of the cost of the goods and the price difference resulting from a failure to make due allowance for delivery costs is not apt to lessen substantially a purchaser's competition with the more favored customer. The one zone system is not apt to cause this type of injury to competition.[140] For this reason it is believed that the independent use of a one zone system by a single seller will not be held illegal under the Clayton Act, unless it shows a monopolistic purpose, which is rather unlikely.

If the theory, apparently accepted by the Supreme Court, that the customer located close to the plant has a natural right to a delivered price advantage over more distant customers is utilized by the Commission, a concept of injury to competition among purchasers might result under which only the f.o.b. mill formula could escape. In both the basing point and the zone type systems the nearby customer is deprived of this right. An individual seller who independently absorbs

[140] "It is not probable that competition among a seller's customers will be injured by the fact that they all acquire goods at the same delivered cost." *Ibid.*

freight to meet distant competition deprives the nearby buyer of this right. Under this theory it would be reasoned that if each buyer was charged the same mill price plus actual transportation costs the buyers located close to the plant would receive a lower delivered price and thus would be better able to compete with the distant buyer whose delivered costs would be higher. Conversely, it could be reasoned that to deprive the nearby buyer of this advantage is to prevent his competing with the favored purchaser who has received a lower price than he would have otherwise. This would seem to be a logical extension of the theory of "natural advantage of the nearby customer." However, the Commission has developed this concept of injury to competition in only the *Pittsburgh Plus* case and has indicated recently that it sees no injury to competition where the buyer is deprived of this "right" by a single seller and not through concerted action.[141]

If present practice and interpretation are followed, the probability of the individual seller's adherence to the single basing point, multiple basing point, freight equalization, or multiple zone systems being declared illegal will depend upon the likelihood of its producing injury to competition between customers of the seller or the customers of such customers. As has been pointed out, such use of the basing point or multiple zone systems is very apt to produce such injury as to make it illegal under the Clayton Act, while the individual seller's use of the freight equalization system is less likely to cause such an injury to this competition. The individual and independent use of the one zone system, although presumably discriminatory, will not produce such an injury to competition as to make it unlawfully discriminatory under the Clayton Act.

I have discussed at some length the concept of injury to competition on the seller's side which was applied in the *Pittsburgh Plus* and *Cement* cases; I believe that proof of such injury does not necessarily depend upon a showing of collusive or concerted use of the pricing system, but may be proved by showing conscious parallel use of such systems. The only decided case in which this concept of parallel action was applied, however, is one based primarily upon collusive use of

[141] "The Commission has challenged uniform delivered pricing only where there is reason to believe that the practice has been observed generally in the industry with the purpose and effect of eliminating price competition among sellers. The Commission has not challenged the independent maintenance of a uniform delivered price by an individual seller. It has not challenged the maintenance of a uniform delivered price by several sellers except where such pricing practices were accompanied by collusion and had the effect of eliminating competition. A proceeding against this type of individual pricing practice would be appropriate only if the practice expressed a monopolistic purpose on the part of the seller who engaged in it or if it injured competition in a substantial manner among the seller's customers." *Ibid.*

The Chief Economist of the Federal Trade Commission goes a little farther and maintains that the nearby customer has no inherent economic right to a price advantage over more distant customers: "I do not believe in inherent economic rights for anybody. I believe that it is desirable, as a matter of public policy, to accord to the buyer the right to try to get the advantage of location and to prevent sellers from collusively depriving him of that right." He said also that in cases in which the Commission has asserted this right, it "was asserting it was wrong for the buyer not to have a chance to scramble for the right on equal terms with the seller." Corwin D. Edwards, Director, Bureau of Industrial Economics, *Hearings*, *supra* note *13*, at 1366.

the basing point system and decided under the Federal Trade Commission Act.[142] That this concept is applicable also to delivered price systems under the Clayton Act is shown by two recently instituted complaints in which the Commission proceeds against uniform prices within the zones of the multiple zone system on the theory that conscious parallel use of such a system violates Section 2(a), in that the seller's delivered prices do not make due allowance for the costs of delivery, and that the purpose and necessary result of such common discrimination is the elimination of price competition among the discriminatory sellers.[143]

In both cases there is a charge in the first count of the complaint that the respondents engaged in a broad price fixing conspiracy which included the establishment of a zone pricing system. In the second count of the complaint in each case there is a charge that the individual seller violates Section 2(a) by quoting a uniform delivered price.

These cases are important in another respect as they present for direct determination for the first time the question of whether a one zone price is discriminatory within the meaning of Section 2(a). For the first time the issue cannot be decided without a determination of whether the delivered price which does not make due allowance for differences in cost of delivery is discriminatory, and, as a corollary question, whether "price" in such cases can be construed as the mill net return of the seller. In view of the apparent acceptance of these arguments by the Supreme Court in prior cases it seems quite likely that all these questions will be answered in the affirmative.

A contrary result would affect seriously the legal status under the Clayton Act of only the one zone price system. There would still exist differences in the delivered prices of all the other delivered price systems which would seem not justifiable under any provision of the Act.

Since the Federal Trade Commission has declared that it sees no danger to competition among the customers of the seller independently employing the one zone price system, the Commission would need or desire to attack the system only when it expressed a monopolistic purpose or when it was used pursuant to a conspiracy or conscious parallel action. The Commission can effectively attack such uses of the system under the Federal Trade Commission Act either as conscious parallel or concerted action, or as monopolistic oppression.

The Commission likewise can effectively attack the other delivered price systems as unfair methods of competition where the injury is to competition in the primary line through either monopolistic oppression or a cooperative elimination of competition by means of reciprocal price matching.

In fact, it has now become apparent that when the injury caused to competition by the use of a delivered price system is this "cooperative" setting aside of com-

[142] See the discussion of the *Conduit* case *supra*, in which an apparent change of opinion by the Federal Trade Commission on the theory of parallelism of action is pointed out.

[143] Matter of Chain Institute, Inc., Docket No. 4878 (1945); Matter of National Lead Co., Docket No. 5253 (1944).

petition on the seller's side of the market by means of a reciprocal matching of prices, the vulnerability of the system to attack is identical under both the Clayton Act and the Federal Trade Commission Act. Consequently, the conclusions reached as to the legality under the Federal Trade Commission Act of collusive and parallel use of the delivered price systems apply with equal force to the question of the legality under the Clayton Act of such use of the systems.[144]

Since the Commission can secure effective relief by proceeding under the Federal Trade Commission Act when injury to competition in the primary line results from the use of the delivered price systems, it would undoubtedly help to clear up much of the existing confusion if the Commission would in such cases confine its actions to the Federal Trade Commission Act and proceed under the Clayton Act only when competition in the second or third lines has been affected.

V

THE NEED FOR LEGISLATION

The recent delivered pricing cases have given rise to a strong movement for the enactment of legislation to clarify the confused state of the law as to the legality of the various pricing systems and practices.

Many businessmen contend that the law pertaining to geographic pricing practices is so uncertain that the only practical pricing method left to them is the f.o.b. mill formula. Any other method is said to involve unreasonable risks for two reasons: (1) a meeting of competition will be labeled a price fixing conspiracy, and (2) a seller cannot absorb freight to reach a market in which he is at a disadvantage freightwise without being found guilty of unlawful price discrimination.

The first reason advanced for the necessity of adopting an f.o.b. mill formula is predicated upon the assumption that the Federal Trade Commission may not be able to distinguish price identities arising from conspiracy or collusion from those arising from competition. The Commission is not limited to an examination of the price identities to determine if sellers have conspired, however, but may look at the movement of prices in relation to each other and at the long run rigidity or flexibility of prices.

In addition to the study of prices and their movements, the Commission, as has been pointed out, has almost always relied upon agreement to establish the system, cooperative activities to make it function, and disciplinary measures to secure adherence to it, to prove conspiracy.

It is, of course, true that the Commission did not rely upon conspiracy in the second count of the *Conduit* case, and that the parallelism of action was not proved in this manner. The existence of tacit conspiracy was so apparent there, however, that it is unrealistic to charge that the Commission mistook competitive action for collusive practices. Indeed, it is submitted that the behavior of prices and of sellers so deviates from the competitive norm where there is collusion or conspiracy, tacit

[144] See pp. 197-200 *supra*.

or overt, that the probability of the Commission's confusing the two, especially after a careful investigation, is so very slight that a businessman who honestly desires to compete and who wishes to refrain from collusive action is in no real danger of being accused of such action by the Federal Trade Commission.

In analyzing the contention that legislation is necessary to allow a seller to absorb freight several facts should be kept in mind: (1) It should be understood that a seller can absorb freight without adhering to one of the delivered price systems which I have considered; (2) it should be recalled that the Supreme Court's condemnation of *systematic* discrimination came in the *Cement* case under such circumstances that the sellers' *systematic* discriminations were actually conscious efforts to match prices pursuant to a conspiracy to eliminate price competition among sellers;[145] (3) the only cases to reach the Supreme Court in which the Section 2(b) defense of a good faith meeting of competition was involved had to do with situations in which there was a collusive matching of prices, or in which the seller was adhering rigidly to a basing point system and thus doing far more than meeting the actual competition of a competitor; (4) the Supreme Court has not yet held that the Section 2(b) defense is not a substantive one and it may not do so; (5) neither has it held that an individual seller cannot absorb freight as a business practice where his independently and competitively arrived at price plus transportation charges is too high to compete with that of another seller. Of course the argument can be raised that if freight absorption is practiced by several sellers the Federal Trade Commission will confuse the resulting price identities as evidence proving a conspiracy. As pointed out above, however, this is thought to be no real or serious danger.

If the Supreme Court upholds the Commission's interpretation of Section 2(b) of the Clayton Act as embodied in its complaint and findings in the *Standard Oil* case, particularly its contention as to who must prove injury to competition, a much better case can be made for the desirability of "clarifying" legislation to define more clearly the rules as to freight absorption. As long as the Commission must bear the burden of proof as to the effect upon competition, the individual competitive seller would incur no great risk in absorbing freight to sell in distant markets, regardless of the nature of the defense of meeting competition in good faith.

We can conclude then that where the seller is not adhering to a basing point or zone pricing system, he is reasonably safe in absorbing freight to meet competition. We have seen that the one zone system is relatively safe because of the improbability of its use producing an adverse effect upon competition. Since, however, the illegality of a price discrimination depends upon its effect upon competition, there can be no complete assurance that any pricing practice other than f.o.b. mill pricing cannot be successfully challenged under the amended Clayton Act. This does not mean, however, that businessmen must adopt an f.o.b. mill

[145] The Court also spoke of systematic discrimination in the *Glucose* cases (see pp. 213, 219 *supra*), but there there was rigid adherence to a single basing point system involving both freight absorption and phantom freight, in an industry in which there was a background of conspiracy.

formula in order to escape an unreasonable risk of being held guilty of an injurious and illegal price discrimination. They can still absorb freight without violating the law if they use reasonable care to avoid price discriminations which are injurious to customers, and if they are reasonably prompt to correct discriminations upon receiving customers' complaints that such injury is being inflicted.

The fact that legislation may not be needed to "clarify" the legal status of freight absorption is not conclusive of the question as to the need for a general legislative overhauling or revision of the antitrust laws. It may well be desirable to examine the antitrust laws in the light of present day conditions and to consider if they are adequate to implement and enforce those policies which are necessary to maintain that type of economy which best serves the public interest.

Such an examination must, however, be conducted in a more objective, public-spirited, and thorough manner than the recent delivered pricing investigations. All viewpoints must be heard, and all interests must be represented, but the proceedings must be as free as possible from the dominance of any self-serving pressure group. Until such an approach to the problem of reformulating antitrust policy can be made, I feel that any attempt to alter the present antitrust policy through legislation is very apt to result in an even further frustration of attempts to preserve that type of economy which is considered to be in the best interests of the country.

THE IMPLIED CONSPIRACY DOCTRINE AND DELIVERED PRICING

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An important weapon in the Federal Trade Commission's attack on industry-wide use of delivered pricing methods has been the doctrine of implied conspiracy, more recently called the doctrine of "conscious parallelism of action."[1] Other weapons have been the definition of "price" as the seller's "mill net return,"[2] denial of a seller's right to meet competitive prices "systematically"[3] (or where such meeting results in injury to competition),[4] and *direct* proof of collusion among competitors in the adoption, continued use, or alteration of a delivered pricing method.[5]

The trend of advancement of the "conscious parallelism of action" doctrine by the Commission, with considerable recognition if not approval by reviewing courts, has now reached a crucial point. Unless the Federal Trade Commission changes

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[1] The term appears in the Federal Trade Commission's published NOTICE TO THE STAFF: IN RE COMMISSION POLICY TOWARD GEOGRAPHIC PRICING PRACTICES, Oct. 12, 1948, p. 3.

[2] The Robinson-Patman bill contained such a definition of "price," but it was withdrawn by the House Judiciary Committee, 80 CONG. REC. 8102, 8140, 8224 (1936). However, Walter B. Wooden, as Associate General Counsel for the Commission, tried to argue the definition back into the law by another route—namely, the argument that sellers are not merely permitted but affirmatively *required* to make "*only* due allowance" for common carrier transportation costs in arriving at delivered prices. CCH, ROBINSON-PATMAN ACT SYMPOSIUM, SECTION ON FOOD, DRUG AND COSMETIC LAW OF THE NEW YORK STATE BAR ASS'N 79 *et seq.* (1946). This means that the seller must add to his mill price only the exact amount of common carrier transportation cost, no more and no less. Some support for the "mill net return" method of measuring discrimination appears by way of *dictum* in the Supreme Court's opinion in Federal Trade Comm'n v. Cement Institute, 333 U. S. 683, 722, 725-726 (1948), wherein the Court stated: "The Commission held that the varying mill nets received by respondents on sales between customers in different localities constituted a 'discrimination in price between different purchasers' within the prohibition of Section 2(a) . . ."; and later: "We hold that the Commission properly concluded that respondents' pricing system results in price discriminations." The Commission now says it has not necessarily espoused the "mill net" theory. NOTICE TO THE STAFF, *supra* note 1, at 5, 6. See also Dawkins, *Defenses Available in Cases of Geographic Price Discriminations*, 37 GEO. L. J. 217, 218 *et seq.* (1949). But its legal staff still uses the theory in its briefs in pending cases. See letter from Kittelle to William Simon, February 21, 1949, in *Hearings before the Subcommittee of Senate Committee on Interstate and Foreign Commerce on S. 236*, 81st Cong., 1st Sess. 325 (1949).

[3] Federal Trade Comm'n v. Cement Institute, 333 U. S. 683, 723-724 (1948); *cf.* Federal Trade Comm'n v. A. E. Staley Mfg. Co., 324 U. S. 746, 755-757 (1945).

[4] Standard Oil Co. v. Federal Trade Comm'n, 173 F. 2d 210 (C. C. A. 7th 1949).

[5] There was such evidence in both Federal Trade Comm'n v. Cement Institute, *supra* note 3, and Triangle Conduit & Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *aff'd per curiam sub nom.* Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949), popularly known as the *Rigid Steel Conduit* case.

its policy, or the courts reject the Commission's theories, or Congress takes remedial action, vigorous, informed, geographical competition will no longer be able to exist except under the shadow of threatened litigation.[6]

It is the purpose of this article to discuss the development, use, and potential future availability to the Commission (and the Commission's trial attorneys) of the doctrine of implied conspiracy or "conscious parallelism of action," and to do so it is first necessary to define the term.

The term "conscious parallelism of action" is a label for a legal theory which represents a radical extension of a principle of law which is accepted without question; that is, that cases may be proved by circumstantial evidence. The phrase appears to have been coined by the Federal Trade Commission in the following context:[7]

In the *Rigid Steel Conduit* case, the Commission found, and the circuit court agreed, that adherence to an industry-wide basing point formula, with the knowledge that other concerns are adhering to it also, constitutes in itself a violation of the Federal Trade Commission Act by the individual adhering companies when price competition is thereby eliminated. It would have been possible to describe this state of facts as a price conspiracy on the principle that, when a number of enterprises follow a parallel course of action in the knowledge and contemplation of the fact that all are acting alike, they have, in effect, formed an agreement. Instead of phrasing its charge in this way, the Commission chose to rely on the obvious fact that the economic effect of identical prices achieved through conscious parallel action is the same as that of similar prices achieved through overt collusion, and, for this reason, the Commission treated the conscious parallelism of action as violation of the Federal Trade Commission Act. Should the Supreme Court sustain the Commission's view, the effect will be to simplify proof in basing point cases, but to expose to proceedings under the Federal Trade Commission

[6] "In my opinion, anyone who uses freight absorption, zone prices, or an individual universal delivered price system, operates under the shadow of illegality and certainly is taking a calculated risk. . . . It is reasonable to say that 118,952 business enterprises will be concerned with these decisions." Commissioner Lowell B. Mason, in *Hearings before the Subcommittee of Senate Committee on Interstate and Foreign Commerce on S. Res. 241*, 80th Cong., 2d Sess. 66-67 (1948).

[7] NOTICE TO THE STAFF: IN RE COMMISSION POLICY TOWARD GEOGRAPHIC PRICING POLICIES, *supra* note 1, at 3. Since the publication of this statement, a staff attorney for the Commission has written to the effect that, in his personal opinion, mere "conscious parallelism of action" without other evidence will not support a finding of conspiracy. Wright, *Collusion and Parallel Action in Delivered Price Systems*, 37 GEO. L. J. 201, 215 (1949). In addition, the report of the subcommittee of the Senate Committee on Interstate and Foreign Commerce which investigated delivered pricing questions concluded that the Commission "appears to have written off the theory that 'conscious parallel action,' absent conspiracy, constitutes an unfair method of competition. . . ." SEN. DOC. No. 27, 81st Cong., 1st Sess. 62 (1949). Yet, Walter Wooden, Associate General Counsel of the Commission, in a letter to the Honorable Wright Patman, member of Congress, dated June 8, 1949, and published by Congressman Patman in a release from his office dated June 14, 1949, made the following statement regarding S. 1008 (then pending before the House): "The first section of the bill is frankly conceded by its author to be intended to cancel the law of Count II of the *Rigid Steel Conduit* case [see discussion of this case, *infra*] and there is little doubt that it does so. The result is that there would be no way of challenging a basing point system except by establishing collusion in its operation. That would relegate us to the 50-year-old test of the Sherman Act and destroy the philosophy of 35 years' standing that the Commission was created to arrest restraints of trade in their incipiency. . . . Unless the concept of incipient restraint of trade can be applied to the basing point method of pricing the concept is an empty one and the Commission loses the thing which differentiates it from the Department of Justice as a 'remedial agency.'" There seems to have been little doubt in Mr. Wooden's mind that absent legislation to the contrary the doctrine of "conscious parallelism of action" is or should be the law.

Act only courses of action which might be regarded as collusive or destructive of price competition.

Although the term "conscious parallelism of action" is used frequently throughout this article, too much attention should not be centered on the phrase itself. As will be shown, the Commission formulated the theory long before it applied the label, and for reasons of expediency the label may, in the future, be discarded by the Commission without abandonment of the theory. Because the term "implied conspiracy doctrine" is such a broad one, however, it is convenient to use the Commission's coined phrase throughout this article to mark off for examination the extreme segment of that doctrine as the Commission's attorneys would apply it.

It seems clear that direct proof of agreement among competitors to adopt, use, or alter[8] a delivered pricing method will support an order to cease and desist from such agreement and from any similar agreement.[9] It is also elementary law that agreement or conspiracy may be proved by circumstantial as well as by direct evidence.[10] Throughout its history the Federal Trade Commission has been permitted to rely upon inference in conspiracy cases.[11] In principle, the doctrine of implied conspiracy may be no more than the doctrine that conspiracy may be found from circumstantial evidence. However, the Commission is now seeking to apply the doctrine far beyond previous uses, producing a trend which, if unchecked, will require no evidence of "conspiracy" in delivered pricing cases beyond the common use in an industry of a delivered pricing method, plus common knowledge of such use, plus substantial uniformity of published (list) prices.[12]

I

History of Doctrine

The evolution of the doctrine of "conscious parallelism of action" has been a gradual one. Initially, the Commission's and its attorneys' approach to delivered pricing appears to have been on the theory that it was a discriminatory and "monopolistic" practice, but not necessarily a collusive practice. The "monopolistic" theory is based on the argument that, under delivered pricing, certain phenomena

[8] In the *Cement* case, pledges were secured by the Institute from its members not to sell f.o.b. mill to purchasers' trucks, and there were other findings of actual collusion (as distinguished from non-collusive identity of action) with respect to the maintenance and operation of the basing point system. In the *Rigid Steel Conduit* case, the question whether Chicago should be continued as a basing point was collectively discussed; in fact, Chicago was originally made a basing point at a 1930 meeting of the Association. There was also collective action to eliminate the Evanston basing point.

[9] The order may also prohibit the respondents from entering into, continuing or carrying out any "planned common course of action." The significance of this phrase is discussed *infra*.

[10] Eastern States Retail Lumber Dealers Ass'n v. United States, 234 U. S. 600, 612 (1914).

[11] Federal Trade Comm'n v. Pacific States Paper Trade Ass'n, 273 U. S. 52 (1927).

[12] The requisite effect (*i.e.*, restraint of trade) is presumed by the Commission, based upon its economic argument (discussed *infra*) that systematic *industry-wide* use of a common delivered pricing method stifles price competition among those using it. Knowledge of such effect on the part of the users of the method may also be presumed (according to the Commission's theory), since a man is held to contemplate the "logical" consequences of his acts. That the consequences may not appear logical to him is, of course, immaterial if the Commission thinks they are so and can persuade the courts to agree.

(*e.g.*, identity of prices and rigidity of prices) may appear, and that these phenomena are also observable in instances of monopoly. The argument seems to run that anything which has the effects of monopoly is tantamount to monopoly and should be unlawful.[13] This, and the argument that delivered pricing is discriminatory, were the chief bases on which representatives of the Commission, during the 1930's and early 1940's, sought legislation outlawing delivered pricing.[14]

Whether the Commission attacks industry-wide delivered pricing as "monopolistic" on the theory that it produces the effects of monopoly, or as "collusive" on the theory that it produces the effects of a conspiracy would seem unimportant. An effective conspiracy is tantamount to monopoly in the economic sense that it produces the effects of monopoly. The distinction between the "monopolistic" and the "collusive" approach to delivered pricing is important only in evaluating the historical development of the "conscious parallelism of action" doctrine and showing that its adherents are fundamentally interested in an end and not in the means used to achieve it.

The *Cement* case[15] was the first attempt by the Commission to strike at delivered pricing on a theory of conspiracy,[16] and a number of subsequently instituted cases were brought on the same theory.[17] In all of these cases, however, an attempt was made by the Commission's attorneys to introduce evidence of conspiracy, *i.e.*, evidence beyond the mere common use of a delivered pricing method with common knowledge of such use and uniformity of prices.[18] Such evidence as was introduced gave rise to specific findings of conspiracy, beyond mere "conscious parallelism of action," by the Commission,[19] and where these findings were reviewed, the courts affirmed them as supported by substantial evidence as required

[13] See findings of Commission, United States Steel Corporation, 8 F.T.C. 1 (1924); statements of Commissioner R. E. Freer, in *Hearings before Senate Committee on Interstate Commerce on S. 4055*, 74th Cong., 2d Sess. 309 *et seq.* (1936); THE BASING POINT PROBLEM 4 (TNEC Monograph 42, 1941).

[14] Statement of R. E. Freer, *Hearings*, *supra* note 13; THE BASING POINT PROBLEM, *supra* note 13.

[15] Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948).

[16] It also contained a count charging price discrimination under the Robinson-Patman Act.

[17] Bond Crown & Cork Co. v. Federal Trade Comm'n, 176 F. 2d 974 (C. C. A. 4th 1949); Allied Paper Mills v. Federal Trade Comm'n, 168 F. 2d 600 (C. C. A. 7th 1948), *cert. denied*, 336 U. S. 918 (1949); Triangle Conduit & Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *aff'd per curiam sub nom.* Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949); Keasbey & Mattison Co. v. Federal Trade Comm'n, 159 F. 2d 940 (C. C. A. 6th 1947); Fort Howard Paper Co. v. Federal Trade Comm'n, 156 F. 2d 899 (C. C. A. 7th 1946), *cert. denied*, 329 U. S. 795 (1946); Milk & Ice Cream Can Institute v. Federal Trade Comm'n, 152 F. 2d 478 (C. C. A. 7th 1946); United States Maltsters Ass'n v. Federal Trade Comm'n, 152 F. 2d 161 (C. C. A. 7th 1945); Eugene Dietzgen Co. v. Federal Trade Comm'n, 142 F. 2d 321 (C. C. A. 7th 1944); American Chain & Cable Co. v. Federal Trade Comm'n, 139 F. 2d 622 (C. C. A. 4th 1944); Phelps Dodge Refining Corp. v. Federal Trade Comm'n, 139 F. 2d 393 (C. C. A. 2d 1943); Salt Producers Ass'n v. Federal Trade Comm'n, 134 F. 2d 354 (C. C. A. 7th 1943).

[18] An exception is the second count of the *Rigid Steel Conduit* case, discussed *infra*; but treating the case as a whole without separation as to counts, evidence of conspiracy was introduced, and a conspiracy was found as to all respondents except two. The first count was dismissed as to these two, but they were found to have engaged in an unfair method of competition under the second purely by reason of "conscious parallelism of action."

[19] For example, see note 8 *supra*.

by the statute.[20] Thus, to date, representatives of the Commission are almost correct when they state that no case has yet been decided by the Commission or courts in which delivered pricing has been outlawed as a collusive practice in the absence of evidence of conspiracy beyond that required by the "conscious parallelism of action" doctrine.[21]

The first effort of the Commission to introduce the doctrine of "conscious parallelism of action" into its cases was an indirect one. The cease and desist order issued by the Commission in the *Salt Producers* case[22] ordered the respondents to cease and desist from "entering into, continuing or carrying out, or directing, instigating, or cooperating in, any *common course of action*, mutual agreement, combination, or conspiracy" wtih respect to the matters specified in the order, among which was the establishment or maintenance of zone delivered pricing. This was not a case wherein the Commission sought to *prove* conspiracy by evidence merely of common use and knowledge of the delivered pricing method. The complaint specifically charged collusion in the establishment of the zone system, and the respondents filed answers admitting all of the material allegations in the complaint.

Respondents in the *Salt Producers* case obtained review of the Commission's order by the Seventh Circuit Court of Appeals,[23] and, among other things, objected to the phrase "common course of action." The Commission contended that it meant nothing by the phrase except that a "common course of action" related to respondents' "admitted combination,"[24] and the respondents conceded that the Commission could validly prohibit a "common course of action" which was the continuation of a conspiracy or was pursuant to an agreement.[25] Respondents argued, however, that the cease and desist order would be effective to prohibit such activity without the words "common course of action."

The court decided that the disputed phrase should remain in the order but that the word "planned" should be inserted before it, making it read "planned common course of action." The court said that, with this modification, "only illegal *contractual* arrangements will be subject to contempt proceedings. The word 'planned' as here used is intended to cover any 'cooperative' or 'concerted' action by [respondents]. . . ."[26]

Had the words "common course of action" remained unmodified and unexplained in the *Salt Producers* order, it would have been arguable in any action for

[20] The statute requires in terms that the Commission's findings be supported only by "testimony," but this has been construed to mean "substantial evidence." See ATTORNEY GENERAL'S MANUAL ON THE ADMINISTRATIVE PROCEDURE ACT 109 (1947).

[21] CORWIN D. EDWARDS, DOING BUSINESS UNDER THE LAW AS IT NOW STANDS IN DELIVERED PRICING AND THE FUTURE OF AMERICAN BUSINESS 93 (Chamber of Commerce of the United States, 1948); see also SEN. DOC. No. 27, 81st Cong., 1st Sess. 46-63 (1949).

[22] Salt Producers Ass'n, 34 F.T.C. 38 (1941).

[23] Salt Producers Ass'n v. Federal Trade Comm'n, 134 F. 2d 354 (C. C. A. 7th 1943).

[24] *Id.* at 357, n. 4.

[25] *Id.* at 357, n. 3.

[26] *Id.* at 357.

violation of that order that evidence merely of parallel action in the use of a zone pricing system, without more, would establish such violation. The addition of the word "planned" and the definition of that term by the Seventh Circuit Court of Appeals made it apparent that additional evidence would be required, but how much and of what? These questions troubled the respondents in the *Wire Rope* case[27] against whom a cease and desist order was entered, containing the phrase "planned common course of action," shortly after the decision of the court in the *Salt Producers* case.

Respondents in the *Wire Rope* case petitioned the Fourth Circuit Court of Appeals to review the order against them, particularly the phrase above mentioned, and asked that that phrase be further modified so that, in an enforcement action, evidence of a *contemporaneous* agreement to follow the common course of action would be necessary. Those respondents pointed out that if two or more of them should independently decide to continue using the zone delivered pricing method which was found to have been the subject of agreement before the order was issued, they could be charged with following a "common course of action" which was "planned" in the sense that it had once been the subject of agreement, even though it would no longer be "planned" because the decision to continue it would be an independent and non-collusive one. The court refused to modify the order, but in affirming it seemed to indicate that something more than bare identity of action would be necessary as a basis for a compliance action.[28]

A third attempt by industry to escape the uncertain implications of "planned common course of action" failed in the *Cement* case, where the Supreme Court expressly sanctioned use of the phrase.[29]

Whether or not "planned common course of action" and its equivalent "planned concerted action" mean the same thing as "conscious parallelism of action" too

[27] American Chain & Cable Co. v. Federal Trade Comm'n, 139 F. 2d 622 (C. C. A. 4th 1944).

[28] "It does not seem to us that the order needs further clarification. It is of course true that a cease and desist order must be certain and unambiguous in its prohibitive terms because business men must operate under it at their peril . . . [citing cases]. But, there can be no doubt that to sustain a charge of violation of the order in this case it must be shown that the prohibited acts have been performed as the result of an agreement or conspiracy, or as the result of a common course of action, that has been agreed upon or planned between two or more persons. If, as the result of such agreement or plan, the petitioners continue to cooperate in a common course of action which has been found to violate the statute, they make themselves liable to the prescribed penalties; and they have no just cause for complaint if in appraising the evidence in any case the triers of fact seek to determine whether there is any relation or connection between their past illegal acts and the conduct under examination. If such a relation or connection is found it may properly be condemned as a continuance of an unlawful conspiracy. Of course the influence of changed business conditions must be taken into account in reaching a decision; but there is no reason to believe that the Federal Trade Commission will fail in its duty in this respect or that the courts will hesitate to modify or reverse an order that is based on inferences not supported by the evidence." *Id.* at 623-624.

[29] The Court said: "Respondents have objected to the phrase 'planned common course of action' in the preamble. The objection is twofold; first, that it adds nothing to the words that immediately follow it; and second, that if it does add anything, 'the Commission should be required to state what this novel phrase means in this order and what it adds to the four words.' It seems quite clear to us what the phrase means. It is merely an emphatic statement that the Commission is prohibiting concerted action—planned concerted action. The Commission chose a phrase perhaps more readily understood by businessmen than the accompanying legal words of like import." 333 U. S. 683, 728 (1948).

closely resembles the famous debates on how many angels can stand on the point of a pin.[30] Suffice it to say that as a result of the *Salt Producers*, *Wire Rope*, and *Cement* decisions, and the inclusion in most Federal Trade Commission orders in conspiracy cases of the phrase "planned common course of action," no respondent who is subject to a cease and desist order in a case in which conspiracy to use a delivered pricing method has been found can afford the risk of continuing the particular delivered pricing method, no matter how independently he arrives at his decision to do so and no matter how lawful the independent use of that type of delivered pricing method might otherwise be. To that extent, at least, the doctrine of "conscious parallelism of action" is already the law.

Where, however, the Commission is not proceeding for the enforcement of an order against respondents already found to have conspired, but is seeking to establish initially that a delivered pricing method was collusively created or used, different considerations presently prevail; and determination of the status in the law of the doctrine of "conscious parallelism of action" requires careful appraisal. It will be apparent from such appraisal that the only thing that is clear is that the Commission has sought to make this doctrine the law.[31]

The best known example of an attempt to make the doctrine of "conscious parallelism of action" the law is the recent *Rigid Steel Conduit* case.[32] There, the respondents were charged in two counts, one for conspiracy and the other for the common use, with common knowledge of such use, of a basing point system. Evidence was introduced under the first count upon the basis of which the Commission found a conspiracy, and on review by the Seventh Circuit Court of Appeals the court said, "We think there was *direct proof* of the conspiracy. . . ."[33] The second count, however, did not purport to charge conspiracy as such, but only "conscious parallelism of action," and the Commission concluded, in effect, that by their individual use of the basing point system, with individual knowledge of its common use throughout the industry, each respondent had engaged in an unfair method of competition in violation of the Federal Trade Commission Act.[34]

The Commission's cease and desist order in the *Rigid Steel Conduit* case, in addition to provisions prohibiting any further combination, conspiracy, or "planned common course of action," also contained a paragraph prohibiting each individual respondent from using the basing point system previously used or any other method of delivered pricing which would produce the effects of price uniformity or varying "mill net returns" on sales to differently located customers.[35]

[30] In the cease and desist order in the *Rigid Steel Conduit* case, the phrase "planned common course of action" appears in the preamble to the Count I portion of the order, whereas the phrase "conscious parallelism of action" was coined to describe the theory of Count II.

A few recent complaints have included the charge of engaging in a "common course of action." National Lead Corp., Docket No. 5253; American Iron & Steel Institute, Docket No. 5508.

[31] NOTICE TO STAFF: IN RE COMMISSION POLICY TOWARD GEOGRAPHIC PRICING PRACTICES, *supra* note 1.

[32] Triangle Conduit & Cable Co. v. Federal Trade Comm'n, 168 F. 2d 157 (C. C. A. 7th 1948), *aff'd per curiam sub nom.* Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949).

[33] *Id.* at 180. (Italics supplied.)

[34] Rigid Steel Conduit Ass'n, 38 F.T.C. 534 (1944).

[35] "It is further ordered that each of the . . . respondents . . . do forthwith cease and desist from

Under pressure of a legislative inquiry into the confused state of the law on delivered pricing, representatives of the Commission sought to rationalize this paragraph in the *Rigid Steel Conduit* order merely as an appropriate remedy to dissipate the effects of an actual conspiracy proved by direct evidence.[36] Considerable emphasis was placed by these spokesmen on the fact that the *Rigid Steel Conduit* case was not one in which the Commission had relied solely on "conscious parallelism of action" but one in which (under the first count of the complaint) both direct and circumstantial evidence beyond mere "conscious parallelism of action" had been adduced.[37]

This attempt in the legislative forum to renounce the "conscious parallelism of action" doctrine *ab initio* was weakened by several factors: (1) the fact that two respondents (Spang-Chalfant, Inc. and Clifton Conduit Company) were exonerated by the Commission from any charge of conspiracy under the first count of the *Rigid Steel Conduit* complaint but were nevertheless held to have engaged in an unfair method of competition under the second count by reason of their individual use of the basing point system with knowledge that other respondents were also using it; (2) the Commission's language on page 3 of its October 12, 1948, statement of "Commission Policy Toward Geographic Pricing Practices"; and (3) statements to the Supreme Court in the *Rigid Steel Conduit* case to the effect that no issue of conspiracy was presented by the second count of the complaint or by the portion of the cease and desist order which required the respondents *individually* to refrain from delivered pricing.[38]

The Seventh Circuit Court of Appeals had affirmed the Commission's findings and order, in their entirety, in the *Rigid Steel Conduit* case, and, unfortunately for

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doing any of the following things for the purpose or with the effect of systematically matching delivered-price quotations with other of said respondents or producing the equivalent of such matched delivered prices through systematic discriminations in the mill nets received on sales to different purchasers:

"(a) Quoting or selling rigid steel conduit at prices calculated or determined pursuant to, or in accordance with, the basing-point delivered-price system.

"(b) Quoting or selling rigid steel conduit at delivered prices calculated as, or systematically equivalent to, the sum of the price in effect at, plus a transportation charge factor from, any point other than the actual shipping point.

"(c) Quoting or selling rigid steel conduit at delivered prices which systematically reflect the inclusion of a transportation factor greater or less than the actual cost of transportation from point of shipment to destination.

"(d) Discriminating among purchasers by quoting or selling rigid steel conduit at prices which systematically differ in terms of mill nets according to the location of purchasers, and which mill nets, plus common carrier transportation charges to the respective locations of such purchasers, produce delivered costs identical with those to such purchasers from differently located respondents." 38 F.T.C. 534, 595-596 (1944).

[36] *Hearings before the Subcommittee of the Senate Judiciary Committee on S. 1008*, 81st Cong., 1st Sess. 70 (1949).

[37] See Sheehy, *The Legal and Factual Content of Recent Geographic Pricing Cases*, 37 GEO. L. J. 183, 193-196 (1949).

[38] 17 U. S. L. WEEK 3293, 3295 (1949). See also Brief for Federal Trade Comm'n, pp. 2, 21, 33, Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949). However, the Government in its brief did hold in reserve the contention that if the Court found the Commission lacked authority so to deal with *individual* conduct, the controverted portion of the order was justified as a means of effectively dissipating the consequences of the conspiracy. *Id.* at 3.

those who hoped for a definitive clarification of the law on delivered pricing, the Supreme Court, by reason of the disqualification of one of its members and the equal division of the others, affirmed the Circuit Court's decision *per curiam*, without opinion.[39]

Thereafter, the respondents moved the Commission to reopen the proceeding and modify the paragraph prohibiting individual delivered pricing, which motion the Commission denied.[40] Thus the Commission's order stands, but weakened by the Commission's own comments.[41]

II

THEORIES ADVANCED IN SUPPORT OF DOCTRINE

Upon what legal or other authorities did the attorneys for the Federal Trade Commission seek to construct the doctrine of "conscious parallelism of action"? A study of their briefs, public statements, and statements before Congressional committees, as well as certain court decisions, discloses that they relied upon a combination of the following:

(1) their economic arguments before Congress during the 1930's and early 1940's that basing point systems are "monopolistic" because they are accompanied by a rigidity and uniformity of prices which might also be found under conditions of monopoly;[42]

(2) their argument that the case of *Federal Trade Commission v. Beech-Nut Packing Co.*[43] establishes the principle that the Commission can find an unfair method of competition in an individual action which restrains trade even though it falls short of conspiracy;[44] and

(3) an attempt to draw an analogy between "conscious parallelism of action" in the industry-wide use of delivered pricing and the factual situations which impelled the courts to find the existence of conspiracies in restraint of trade in *Interstate Circuit v. United States*,[45] *Bigelow v. RKO Radio Pictures*,[46] and *William Goldman Theatres, Inc. v. Loew's, Inc.*[47]

[39] 336 U. S. 956 (1949).

[40] Rigid Steel Conduit Mfgrs., CCH TRADE REG. SERV. ¶14 (Docket No. 4452, 1949). The order stated in part: "The purpose of the requested modification is said to be to make clear that the order does not prohibit any of the respondents, acting independently, from quoting or selling at delivered prices or from absorbing freight. The Commission does not consider that the order in its present form prohibits the independent practice of freight absorption or selling at delivered prices by individual sellers. What the questioned portion of the order does prohibit is the continuance of the basing-point, delivered price system, found to have been the subject of conspiracy, or any variation thereof which might be accomplished through the practices specified in subparagraphs (a), (b), (c), or (d) when done, as stated in the order, 'for the purpose or with the effect of systematically matching delivered price quotations.'"

[41] SEN. Doc. No. 27, 81st Cong., 1st Sess. 62 (1949). See also portion of order quoted note 40, *supra*.

[42] See statement of Commissioner R. E. Freer, and TNEC Monograph 42, note 13, *supra*.

[43] 257 U. S. 441 (1922).

[44] Sheehy, *supra* note 37, at 194.

[45] 306 U. S. 208 (1939).

[46] 150 F. 2d 877 (C. C. A. 7th 1945), *rev'd* on grounds not pertinent to this article, 327 U. S. 251 (1946).

[47] 54 F. Supp. 1011 (E. D. Pa. 1944), *rev'd*, 150 F. 2d 738 (C. C. A. 3d 1945), *cert. denied*, 334

Analysis of these economic arguments and decisions shows that they will not logically support the claim that "conscious parallelism of action" in the use of delivered pricing methods is, without more, either an unfair method of competition apart from conspiracy or sufficient evidence in and of itself of a conspiracy.

The argument that basing point systems are "monopolistic" because accompanied by price uniformity and rigidity often found in conditions of actual monopoly is necessarily based upon two theories: first, that uniformity and rigidity of prices in basing point industries are caused by the basing point system and not by something else; and second, that uniformity and rigidity of prices must be regarded as evidence of conspiracy or of a monopolistic condition, rather than as evidence of competition, or at least evidence which may point impartially either way and which should be regarded as inconclusive in the absence of other evidence.

The very fact that representatives of the Commission claim (with considerable accuracy) that every delivered pricing case decided to date by the Commission or courts (except those based entirely on the Robinson-Patman Act) has included substantial evidence, or admissions by the respondents, of actual collusion to fix prices, should suggest to the Commission that the cause of such price uniformity and rigidity as was found in those cases was not the delivered pricing method but the price-fixing conspiracy. As a matter of logic, it seems difficult to envision how a simple delivered pricing method such as freight equalization[48] or "universal delivered pricing"[49] could, in and of itself, without outside assistance in the form of

U. S. 811 (1948) (same case, 164 F. 2d 1021 (C. C. A. 3d 1948)). (Here, as will be seen *infra*, the decision technically did not rest on conspiracy but upon monopoly.)

[48] By this term the writers refer to the practice of each (and every) manufacturer in an industry quoting a price f.o.b. his mill and being willing to sell at that price to any buyer who wishes to buy at the mill, whether in a truck or otherwise. Up to this point the practice would not offend the most ardent proponent of strict f.o.b. mill pricing. However, in order to be free automatically to sell in territories closer to competitors' plants and to have a quoted list price readily available for such sales, each manufacturer announces on its price list that it will "equalize freight" with any competing plant. This means that the buyer pays the manufacturer's f.o.b. mill price and pays the carrier its full, actual charge for transportation to destination. However, if such charge is greater than it would have been from some competitor's mill which is closer freightwise to the buyer, then the buyer receives an allowance in the amount of the difference. The foregoing description assumes that the f.o.b. mill prices of all manufacturers are uniform. If they are not, the manufacturer will have to do more than merely "equalize freight." In such case, if his f.o.b. mill price plus actual freight to the buyer is higher than the f.o.b. mill price of any competitor, plus freight from that competitor's mill to the buyer, the manufacturer will give the buyer an allowance in the amount of the difference. It is noteworthy that Corwin D. Edwards, Chief Economist of the Federal Trade Commission, sees little danger of concentration of economic power under "freight equalization," or under "universal delivered pricing" described *infra*, note 49. See Edwards, *Geographic Price Formulas and the Concentration of Economic Power*, 37 GEO. L. J. 135, 147 (1949).

[49] By this term the writers refer to the practice of a manufacturer charging the same price delivered at any destination in the United States. This is sometimes called the "postage stamp" method of selling and is common in the case of many articles of consumer goods where freight is not an important element of the price. The Commission is itself on record that this method of selling creates no inference of collusion, even in the parallel action of a number of competitors, where the use of the method and the uniformity of delivered prices have "simple and logical explanations in the nature of the market, the product, and the transportation cost." See FTC, NOTICE TO THE STAFF, IN RE COMMISSION POLICY TOWARD GEOGRAPHIC PRICING PRACTICES 4 (October, 1948). See also FTC, PRICE BASES INQUIRY: THE BASING POINT FORMULA AND CEMENT PRICES 13 (1932).

either (1) a price-fixing agreement, (2) price leadership (lawful[50] or collusive), or (3) the effect of competition on a homogeneous product,[51] produce price uniformity or rigidity. Although such methods of selling enable a seller to meet competitors' prices in distant markets, there is nothing in their operation that anaesthetizes his will and prevents him from beating such competitors' prices where he wishes.

The Commission's argument that industry-wide use of a delivered pricing method in and of itself produces price uniformity and rigidity is analogous to its argument in *Tag Manufacturers Institute v. Federal Trade Commission*.[52] Respondents in that case had a price reporting plan which the Commission condemned. The evidence showed that respondents followed their list prices in 75 per cent of the dollar value of the industry's sales and sold at "off-list" prices in 25 per cent of the dollar value of the industry's sales. Since there was considerable uniformity among respondents' list prices, considerable uniformity prevailed in the 75 per cent of respondents' sales which were at list prices. The Commission found from this evidence that the price reporting plan itself was the cause of such uniformity. As to this, in setting aside the Commission's cease and desist order, the court said:[53]

> . . . The evidence does not . . . warrant the Commission's finding that the effect of the operation of the Tag Industry Agreements "has resulted in a substantial uniformity of prices for tags and tag products among the respondent members." In the first place, this implies that the instances of departure from uniformity are insignificant and unsubstantial—which certainly cannot be said. In the second place, *there is no evidence that such uniformity as has existed is a result of the operation of the Tag Industry Agreements*, for it does not appear whether there has been an increase or decrease of uniformity either in list prices or in actual selling prices since the agreements have been in operation.

It seems significant that, even when arguing before the Temporary National Economic Committee that the basing point system in the steel industry was a "monopolistic practice" which in and of itself produced price uniformity, Walter B. Wooden, then Assistant Chief Counsel, and Hugh E. White, Examiner, of the Federal Trade Commission, were at pains to cite many printed pages of documentary evidence which they claimed showed actual collusion on prices, extras, and delivery charges.[54] Thus, it appears that representatives of the Commission are themselves reluctant to rest on the proposition that delivered price methods of selling have any automatic ability to produce price uniformity.

It is beyond the scope of this article to enter the field of economic argument on the subject of price uniformity and rigidity as evidence of conspiracy. The courts have held that price uniformity may result from lawful price leadership,[55] and in

[50] United States v. International Harvester Co., 274 U. S. 693, 708 (1927).

[51] See Rodgers and Luedicke, *Dynamic Competition*, 27 HARV. BUS. REV. 237, 248 (1949).

[52] 174 F. 2d 452 (C. C. A. 1st 1949).

[53] *Id.* at 460. (Italics supplied.)

[54] THE BASING POINT PROBLEM (TNEC Monograph 42), *supra* note 13, at 93-107.

[55] United States v. International Harvester Co., *supra* note 50; United States v. Standard Oil Co. of New Jersey, 47 F. 2d 288, 316-317 (E. D. Mo. 1931).

a series of questions and answers submitted to the Subcommittee on Trade Policies of the Senate Committee on Interstate and Foreign Commerce, the Federal Trade Commission, through Commissioner Davis, took the following position:[56]

"Q. Do you think that identical prices can result from competition as well as from conspiracy?

"A. Yes."

While it is difficult to see how simple forms of delivered pricing such as "freight equalization"[57] or the "universal delivered pricing" method[58] can logically be accused of causing, in and of themselves, any greater uniformity or rigidity of prices than would exist under any selling method which permitted several sellers to compete in the same market,[59] some forms of basing point pricing may become so complex and rigid in their mechanical workings as logically to produce a greater degree of rigidity and uniformity of prices than would obtain in their absence. This is really the burden of the Commission's objection to "Pittsburgh Plus" in the steel industry;[60] to the multiple basing point system as it existed in the steel industry during the days of T.N.E.C.;[61] and to the multiple basing point systems found in the *Cement* and *Rigid Steel Conduit* cases.[62] However, in instances like these it is likely that evidence of actual conspiracy to hold the system together will be found. As has aptly been said by an attorney on the Commission's staff:[63]

> The necessity for identical transportation factors, for refusing to permit delivery to trucks or water carriers, for preventing "diversion in transit," and for unified action in every other respect in which a price advantage can be created for any seller, makes it unlikely that such a system can be made to produce continued identity of prices *without leaving a trail of evidence sufficient to condemn the venture.*

The second major argument used by attorneys for the Commission in constructing the doctrine of "conscious parallelism of action" is that the *Beech-Nut* case establishes the principle that the Commission can find an unfair method of competition in individual action that falls short of conspiracy. In a footnote to its

[56] SEN. DOC. No. 27, 81st Cong., 1st Sess. 62 (1949).

[57] See note 48 *supra.*

[58] See note 49 *supra.*

[59] Strict f.o.b. mill pricing would logically provide direct price competition only at the boundaries of the various sellers' territories, assuming only one mill at each production point. If two or more competing mills were located at the same point, they would, of course, compete directly throughout their territory, but in such case it seems logical that uniformity of prices would tend to exist among them to the extent that their products were homogeneous. If price uniformity is to be blamed on the pricing method, it could here be blamed upon the f.o.b. mill pricing method. Such method could also be charged with responsibility for the uniformity of price which would be likely to occur at boundaries between competing mill territories. The writers feel, however, that in neither of these instances, nor in the case of the simpler forms of delivered pricing, can the method of selling logically be blamed for a condition which will occur under any method of selling which permits sellers to compete in the same market.

[60] United States Steel Corp., Docket No. 760, *aff'd* by consent Oct. 5, 1948 (C. C. A. 3d 1948).

[61] THE BASING POINT PROBLEM (TNEC Monograph 42, 1941), *supra* note 13.

[62] See Edwards, *supra* note 48, at 135-146, wherein it is apparent that the systems he is describing and criticizing involved non-basing point mills, organized "disciplining" of price-cutters, etc. Compare this with his discussion of "freight equalization" and the uniform delivered price, *id.* at 147.

[63] Wright, *supra* note 7, at 214. (Italics supplied.)

majority opinion in the *Cement* case,[64] the Supreme Court cited the *Beech-Nut* case as authority for the abstract proposition that the existence of a combination is not an indispensable ingredient of an unfair method of competition under the Federal Trade Commission Act. This statement was pure *dictum* because of the categorical holding of the Court that the Commission's findings of combination were supported by evidence.[65]

The *Beech-Nut* case involved a complex system established by the Beech-Nut Packing Company for the purpose of policing violations of its "suggested" resale prices. The earlier decision in *United States v. Colgate*[66] had held that it was lawful for a manufacturer to announce to its dealers suggested resale prices and further to announce a policy of refusing to sell to those dealers who did not comply with the suggestion, so long as no agreement was made and the dealer was free to comply or not, risking only the possibility of being cut off from further supplies by the manufacturer.

The Beech-Nut Company followed the principle of the *Colgate* case but went further. It established a system involving black lists and white lists, encouragement of dealers to report price-cutters, reinstatement of previously cut off dealers upon satisfactory "assurances" that they would comply with the suggested prices in the future, and the general organization of all dealers to cooperate in maintaining the resale price policy of Beech-Nut.

The case was decided upon an agreed statement of facts upon which the Commission felt constrained, for some reason, to make a specific finding that the merchandising conduct of Beech-Nut did not "constitute a contract or contracts whereby resale prices are fixed, maintained or enforced."[67] The reviewing court was thus forced into the position of determining the legality or illegality of the system under the Federal Trade Commission Act, apart from any agreement, notwithstanding that the Commission might well have found that the cooperative activities between Beech-Nut and its dealers did constitute an agreement, combination or conspiracy.

The Court upheld the Commission's conclusion that the Beech-Nut system was an unfair method of competition, but it is noteworthy that the Court regarded the Commission's cease and desist order as too broad and modified it to prohibit only those activities of Beech-Nut which exceeded the simple suggestion of resale prices and announcement of a refusal-to-sell policy, sanctioned by the *Colgate* decision. Thus, the Court, unlike the Commission, was not prepared to deprive Beech-Nut of the independent right to use a lawful selling method merely because its prior use thereof had exceeded the bounds of legality by the addition of other practices involving active cooperation with its dealers.

[64] 333 U. S. 683, 721 n. 19 (1948).
[65] See Justice Burton dissenting, *id.* at 732-733.
[66] 250 U. S. 300 (1919).
[67] 257 U. S. 441, 455 (1922).

There seems little doubt that, in the *Beech-Nut* case, the cooperative activities of Beech-Nut and its dealers were in fact collusive, even though there were no formal written contracts with the dealers such as were condemned in *Dr. Miles Medical Company v. Park & Sons Company*.[68] The Commission's finding that the activities of Beech-Nut and its dealers did not constitute a "contract or contracts" may be taken to mean merely that there were no contracts of the *Dr. Miles* type, and the decision may then be rationalized on the principle that agreements in restraint of trade may readily be implied from evidence as direct as that in the *Beech-Nut* case. If not thus rationalized, the decision would seem to fit only the principle of a hard case making bad law.

A majority of the Federal Trade Commission has taken the public position that:[69]

> Each seller may choose his own method of pricing provided that he does not conspire or agree with his competitors and provided that he does not discriminate in price in the manner prohibited by law and thereby injure competition or tend to create a monopoly. A seller may absorb freight or absorb part of his manufacturing costs or any other costs in order to in good faith meet an equally low price of a competitor.

If an individual seller may do these things, the fact that two or more competing sellers do them independently should not be treated as an unfair method of competition under the principle of the *Beech-Nut* case. If there was evidence of agreement, then the *agreement* would be unlawful and should be prohibited. Evidence of agreement might be spelled out of activities of the respondents beyond the mere common use of a delivered pricing method with consciousness of such common use, just as the activities of Beech-Nut and its dealers beyond the mere announcement by Beech-Nut of suggested prices and a refusal-to-sell policy spelled out what was in essence an agreement, despite the Commission's finding that they did not constitute a "contract or contracts." But, as in the *Beech-Nut* case, the cease and desist order should be modified if it prohibits any respondent from further use of delivered pricing in the absence of agreement or unlawful discrimination in such use. In this respect, it is submitted, the order in the *Rigid Steel Conduit* case went too far.

The third major argument used by attorneys for the Commission in constructing the doctrine of "conscious parallelism of action" is that common, conscious use of the same delivered pricing method by competing members of an industry is analogous to the factual situations which impelled the courts to find the existence of conspiracies in restraint of trade in *Interstate Circuit v. United States*, *Bigelow v. RKO Radio Pictures*, and *William Goldman Theatres, Inc. v. Loew's, Inc.*

The *Interstate Circuit* case arose out of a series of substantially identical contracts between defendant Interstate, an important motion picture exhibitor in Texas, and

[68] 220 U. S. 373 (1911).

[69] SEN. DOC. No. 27, 81st Cong., 1st Sess. 62 (1949).

eight major motion picture distributors.[70] The District Court[71] found that the distributors had conspired among themselves and with Interstate with regard to these contracts, and further that the contracts themselves violated the Sherman Act. Appeal was taken directly to the Supreme Court, which affirmed.[72]

Had the Supreme Court stopped with its holding that the trial court's finding of conspiracy among the distributors was supported by evidence, the case would

[70] Defendant Interstate owned virtually all of the first-run moving picture theatres in six Texas cities. The court found that it and an affiliated company, also a defendant, "dominate the motion picture business in the cities where their theatres are located." In these cities, they were in competition with moving picture theatres that showed Class A pictures in second runs (pictures shown for the second time in the same city), and also pictures below Class A in quality. Interstate generally charged 40 cents admission in its first-run theatres, while competing second-run theatres charged much lower prices, as low as 10 or 15 cents, and also sometimes offered double features.

In July 1934 Interstate's general manager wrote a letter to the local Texas branch managers of the eight major motion picture distributors, stating in substance that Interstate would have to cut its 40-cent admission price unless these distributors agreed that, in licensing their Class A films to second-run theatres in the cities concerned, they would require the latter not to charge less than 25 cents admission and not to run such films as part of any double feature program. The letter was a joint missive addressed to all of the branch managers of the eight distributors, each of whom received a copy of it.

Each of the distributors' branch managers disclaimed authority to make any such agreement with Interstate, and referred the matter to his principal. It appeared that conferences were then held by each distributor separately with Interstate, and eventually each distributor entered into a contract with Interstate embodying substantially the terms of Interstate's demand. There was no direct evidence that the distributors agreed or even conferred among themselves on the subject, but on the other hand no executive officer or other official of the distributors, except the branch managers, appeared as a witness.

[71] 20 F. Supp. 868 (N. D. Tex. 1937).

[72] With respect to the evidence from which the district court drew its inference of conspiracy, the Supreme Court said:

"The trial court drew the inference of agreement from the nature of the proposals made on behalf of Interstate and Consolidated [Interstate's affiliate]; from the manner in which they were made; from the substantial unanimity of action taken upon them by the distributors; and from the fact that appellants did not call as witnesses any of the superior officials who negotiated the contracts with Interstate or any official who, in the normal course of business, would have had knowledge of the existence or non-existence of such an agreement among the distributors. . . ." 306 U. S. 208, 221 (1939).

The Court pointed out that each of the distributors had received a copy of the Interstate letter which named on its face all of the distributors to whom it was sent. With respect to the subsequent unanimity of action by the distributors, the Court said:

". . . It taxes credulity to believe that the several distributors would, in the circumstances, have accepted and put into operation with substantial unanimity such far-reaching changes in their business methods without some understanding that all were to join, and we reject as beyond the range of probability that it was the result of mere chance." *Id.* at 223.

With respect to appellants' arguments that inferences other than that of agreement might be drawn from their acts, the Court said:

". . . we decline to speculate whether there may have been other and more legitimate reasons for such action *not disclosed by the record*, but which, if they existed, *were known to appellants*." *Id.* at 225. (Italics supplied.)

The Court adverted to the fact that appellants had failed to put on the witness stand any officer or person who knew or should have known of the existence or non-existence of any conspiracy among the distributors. It said that when the proof supported the inference of conspiracy the burden of going forward with evidence to explain or contradict it shifted to the appellants, but that they undertook to carry out that burden only by calling as witnesses their local branch managers each of whom testified that *he* had had no conferences with other distributors or their representatives. The Court then said:

". . . The failure under the circumstances to call as witnesses those officers who did have authority to act for the distributors and who were in a position to know whether they had acted in pursuance of an agreement is itself persuasive that their testimony, if given, would have been unfavorable to appellants. The production of weak evidence when strong is available can lead only to the conclusion that the strong would have been adverse. *Clifton v. United States*, 4 How. 242, 247. Silence then becomes evidence of the most convincing character [citing other cases]." *Id.* at 226.

have afforded little or no aid in the construction of the Federal Trade Commission's doctrine of "conscious parallelism of action," although it does, of course, substantiate the undisputed doctrine that conspiracies can be found from circumstantial evidence. The circumstantial evidence in the *Interstate* case involved, however, far more than mere parallel action and consciousness of it in a situation where parallel action is to be expected because induced by the legitimate desire to sell in distant markets and the necessity of meeting competitors' prices in order to do so. The distributors in the *Interstate* case made drastic changes in their business practices as the result of pressure put on them from the outside, *i.e.*, by Interstate. It is noteworthy that, in this part of its opinion, the Court supported the District Court's finding that there had been a conspiracy among the distributors themselves, apart from their independent conferences with Interstate, and did not indicate that in the absence of such a conspiracy, parallel action by the distributors would have been unlawful. In fact, the stress laid by the Court on the absence of testimony by the officers of the distributors implies that had such officers explained away or rebutted the prima facie case of conspiracy created by the circumstantial evidence in the record, the parallel action would have been lawful.

The Court, however, did not stop with its holding that the District Court's finding of conspiracy was supported by the record, but continued with what it is submitted may be characterized as *dictum*;[73] and it is this *dictum* which laid the foundation for the Federal Trade Commission's doctrine of "conscious parallelism of action":[74]

> While the District Court's finding of an agreement of the distributors among themselves is supported by the evidence, we think that in the circumstances of this case such agreement for the imposition of the restrictions upon subsequent-run exhibitors was not a prerequisite to an unlawful conspiracy. It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it. Each distributor was advised that the others were asked to participate; each knew that cooperation was essential to the successful operation of the plan. They knew that the plan, if carried out, would result in a restraint of commerce, which, we will presently point out, was unreasonable within the meaning of the Sherman Act; and, knowing it, all participated in the plan. The evidence is persuasive that each distributor early became aware that the others had joined. With that knowledge they renewed the arrangement and carried it into effect for the two successive years.
>
> It is elementary that an unlawful conspiracy may be and often is formed without simultaneous action or agreement on the part of the conspirators. *Schenck v. United States*, 253 Fed. 212, 213, aff'd 249 U. S. 47; *Levey v. United States*, 92 Fed. 2d 688, 691. Acceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequences of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act. *Eastern States Lumber Assn. v. United States*, 234 U. S. 600; *Lawlor v. Loewe*, 235 U. S.

[73] This is doubly true because, in addition to the holding of conspiracy, the Supreme Court sustained the lower court's judgment and decree upon the ground that each individual contract between a distributor and Interstate was a contract in unreasonable restraint of trade, apart from any conspiracy among the distributors themselves.

[74] 306 U. S. 208, 226-7 (1939).

522, 534; *American Column Co. v. United States*, 257 U. S. 377; *United States v. American Linseed Oil Co.*, 262 U. S. 371.

Certain highlights in the foregoing quotation should be kept in mind. First, the Court said that agreement among the distributors was not a prerequisite to an unlawful conspiracy *"in the circumstances of this case."* Second, the knowledge imputed to the distributors was not mere knowledge that parallel action existed but knowledge that "concerted action was *contemplated and invited*." Third, knowledge was required that the plan, if carried out, "would result in an [unreasonable] restraint of commerce."

Each of these elements would distinguish this case from a situation in which sellers independently and individually elected, for example, to sell at a price which was the same delivered anywhere in the United States or to sell on a basis whereby each equalized or absorbed freight with the others so as to sell in the others' territories. In such a situation, although parallel action would exist, it would not be "invited" and would not necessarily be "contemplated." The condition would not suddenly come into existence as the result of a plan circulated by one of the sellers (or by an outsider) to all concerned. The situation would, moreover, be explainable in the nature of the homogeneity of the product and the necessity for meeting competitors' prices, and there is no reason why the sellers would not take the witness stand, explain their individual and independent actions and the business reasons which motivated them, and thus rebut any inference of conspiracy.

Moreover, in a simple delivered pricing situation of the type described, it could not validly be said that the sellers, although they might know of the parallel action in their industry (such knowledge being hard to avoid by an alert business man), would be chargeable with knowledge that such parallel action restrained trade unreasonably. Any argument to the contrary would have to be based on the Commission's apparent view that price uniformity restrains trade whether it is the result of conspiracy or competition, and the further view that where price uniformity exists under a delivered pricing method, it is the method of selling and not something else that is the operating cause of it. We have already attempted to demonstrate the unsoundness of both theories.

Thus, the *Interstate Circuit* decision does not justify the doctrine of "conscious parallelism of action" as the Commission would seek to apply it, *i.e.*, by proof only of common use and common knowledge of the use of a delivered pricing method in an industry, plus evidence of the uniformity of prices.

Language in the *Bigelow* and *Goldman* cases goes a little further in the direction of the Commission's theory of "conscious parallelism of action" than does the language of the *Interstate Circuit* case, but the cases do not support the theory.

The *Bigelow* case was a suit for treble damages under the Sherman and Clayton Acts based upon an alleged conspiracy among motion picture distributors in Chicago to maintain a distribution system under which minimum admission prices of theatres were fixed, and each theatre was classified as to the period when it might

exhibit feature films.[75] The case was tried before a jury on two alternative and mutually exclusive theories,[76] one being that there was an unlawful conspiracy among the distributor-defendants to maintain the distribution *system*, and the other being that there was an unlawful conspiracy among the distributor-defendants (even though their maintenance of the system might be non-collusive) to discriminate against the plaintiffs' theatre in the matter of its classification. The jury returned a general verdict for the plaintiffs and, on appeal, the Seventh Circuit Court of Appeals undertook, by deductive reasoning, to ascertain upon which of the two theories the jury had based its verdict. The court decided that the jury had based its verdict on the first theory (conspiracy to maintain the system) and that such verdict was supported by the evidence. However, it reversed the trial court's judgment with instructions to enter judgment for the defendants *non obstante veredicto* on the ground that the plaintiffs had not proved damages. Plaintiffs appealed to the Supreme Court, which held that the plaintiffs had proved damages and reversed the judgment of the court of appeals and affirmed that of the district court.

There is nothing in the opinions of either the circuit court of appeals or the Supreme Court which sheds any light on the nature or scope of the evidence which was held to support the jury's verdict of conspiracy to maintain the distribution system.[77] The following statement of the circuit court of appeals is the one relied upon by the Federal Trade Commission as justification for its "conscious parallelism of action" doctrine:[78]

> Knowing participation by competitors without previous agreement in a plan, the necessary consequences of which if carried out is unreasonable restraint of interstate commerce, is sufficient to establish an unlawful conspiracy.

In support of this statement the court cited the *dictum* hereinbefore quoted from the *Interstate Circuit* case. However, without knowing the nature and scope of the evidence which was before the jury, the statement must be regarded as *dictum*, as it was in the *Interstate Circuit* case.[79]

[75] Plaintiffs owned a theatre in a neighborhood section of the city which was in competition with theatres owned by the film distributor-defendants. Plaintiffs' theatre, under the system, was not permitted to exhibit feature films until ten weeks after such films had completed their showing in the downtown Loop section of the city where the theatres were owned by the distributor-defendants. The distribution system was uniform in all of its details among the distributor-defendants, *i.e.*, the same minimum admission prices were required by all distributor-defendants of each class of theatres and their classification of theatres was uniform. Plaintiffs had sought, unsuccessfully, to have their theatre reclassified into a more favorable grouping so it could obtain feature pictures a shorter time after they had been shown in the Loop.

[76] The circuit court of appeals held that the plaintiffs had admitted that the two theories were mutually exclusive, and thus bound themselves by the admission, whether the theories would otherwise have been so regarded or not.

[77] Beyond outlining the general nature of the motion picture industry, the details of the distribution system itself, the fact that all defendants used it, and the evidence regarding plaintiffs' damages, neither court discussed the evidence at all, except that the circuit court of appeals said that ". . . no specific agreement to enter into such conspiracy on the part of the defendants was proven. . . ." 150 F. 2d 877, 882 (C. C. A. 7th 1945). This might, of course, mean only that no direct proof of agreement was made but that there was sufficient circumstantial evidence beyond mere unanimity of action.

[78] 150 F. 2d 877, 882, 883 (C. C. A. 7th 1945).

[79] It is interesting that the circuit court of appeals distinguished two other cases: Gary Theatre Co. v.

It is evident that the decision neither of the circuit court of appeals nor of the Supreme Court[80] in the *Bigelow* case, as written, can be said to have extended, or made into law, the original *dictum* in the *Interstate Circuit* case.

The final case relied upon by the Commission to support its doctrine of "conscious parallelism of action" is the *Goldman* case. Plaintiff Goldman, lessee of a downtown motion picture theatre in Philadelphia, was uniformly refused first-run films by all distributors, although it offered higher rental fees than the single exhibitor (Warner) which controlled all the other downtown theatres.[81]

Plaintiff Goldman brought an action for an injunction and treble damages for violation by the defendants of Sections 1 and 2 of the Sherman Act. The trial court found that, with respect to Section 1, "Uniformity of action . . . without more, is not evidence of agreement or conspiracy."[82] On the question of Section 2, the lower court held, in substance, that while the effect of the distributors' contracts to lease first-run pictures only to Warner was to give Warner a monopoly of such pictures in Philadelphia, a monopoly of so small a part of commerce was not unlawful unless there was an intent to monopolize, which he found did not exist. He therefore entered judgment for defendants, and plaintiff appealed.

Columbia Pictures Corp., 120 F. 2d 891 (C. C. A. 7th 1941) and Westway Theatre v. Twentieth Century Fox Film Corp., 30 F. Supp. 830 (Md. 1940), *aff'd*, 113 F. 2d 932 (C. C. A. 4th 1940) (in which the defendants had also followed an identical distribution system for moving pictures), on the ground that in each of those cases the district court had found no conspiracy and the circuit court of appeals was bound by such finding of fact. If, as a matter of law, "conscious parallelism of action" is tantamount to conspiracy, it would seem illogical to leave the trial courts and juries *carte blanche* discretion to decide either way on the subject. The inference is that in the *Bigelow* case there was at least circumstantial evidence of conspiracy beyond mere "conscious parallel action," while in the *Gary* and *Westway* cases there was either no such additional evidence or evidence negativing any inference of conspiracy.

[80] The decision of the Supreme Court in the *Bigelow* case does not shed much light on the question under discussion. In that Court, the defendants abandoned their attack on the jury's finding of conspiracy, and the sole question was whether the plaintiffs had proved damages. The Supreme Court did say:

"There was evidence from which the jury could have found that respondents maintained in the Chicago district, by a conspiracy among themselves, a discriminatory system of distributing motion pictures for showing in successive weeks of release. . . ." 327 U. S. 251, 255 (1946).

And later it said:

". . . evidence was introduced in the course of the trial tending to show that respondents conspired to maintain the release system as part of a conspiracy to maintain minimum admission prices to be charged by exhibitors generally. . . ." *Id.* at 257.

These statements are, again, some indication that the evidence before the jury went beyond that of mere "conscious parallelism of action."

[81] Distributors of motion pictures controlling the production and distribution of 80 per cent of the feature pictures available for distribution in the United States had contracts with a single exhibitor (Warner Brothers) owning seven first-run motion picture theatres in Philadelphia. These contracts required the distributors to furnish first-run feature pictures only to Warner. Plaintiff, who had been in the motion picture exhibition business in Philadelphia for many years, rented a theatre in downtown Philadelphia suitable for the showing of first-run pictures. Before doing so, plaintiff was informed by one of the distributor-defendants that the latter would very likely lease him first-run pictures because it was dissatisfied with Warner Brothers. However, after renting the theatre, plaintiff applied to all of the distributors for first-run pictures and was uniformly refused by all, notwithstanding that it offered them higher rental fees than Warner Brothers.

[82] 54 F. Supp. 1011, 1013 (E. D. Pa. 1944).

The Third Circuit Court of Appeals reversed the judgment and remanded the case to the district court to take evidence with respect to plaintiff's damages and to formulate an appropriate decree.[83]

The decision of the circuit court of appeals contains somewhat indiscriminate references to both "conspiracy" and "monopoly," but appears clearly to have been based on a rejection of the lower court's holding that a local monopoly is not unlawful without specific intent to monopolize.[84] While Section 2 of the Sherman Act prohibits not only monopolization and attempts thereat but also combinations and conspiracies to monopolize, the decision of the Circuit Court of Appeals can be, and apparently is, rationalized on the theory that the effect of the contracts between the distributors and Warner gave Warner an absolute monopoly of a portion of interstate commerce, *i.e.*, the showing of first-run pictures in Philadelphia, and that the limited nature of the monopoly did not exempt it from the Sherman Act. The court's discussion of conspiracy, therefore, may well be regarded as *dictum*. However, it should not be ignored because it contains language relied upon by the Federal Trade Commission to support its "conscious parallelism of action" doctrine. The precise language is:[85]

> Uniform participation by competitors in a particular system of doing business where each is aware of the other's activities, the effect of which is restraint of interstate commerce is sufficient to establish an unlawful conspiracy under the statutes before us.

As to the conspiracy charge, the court noted that the plaintiff had put on proof of his own ability to operate a first-run theatre, the suitability of his theatre for first-run pictures, and the uniform refusal of each distributor to lease him (or anyone except Warner) first-run pictures. In addition the plaintiff showed that he had served interrogatories on each of the defendant distributors asking why it had refused him first-run pictures, and that their answers were evasive and not factual or responsive. One answered that its arrangement with Warner gave it "economic advantages"; another that it was "more advantageous"; a third that it was "desirable"; and a fourth that it was "very satisfactory"—this in spite of the fact that plaintiff had offered them more money for first-run pictures than Warner.

In view of this evidence,[86] the *Goldman* case, it is submitted, cannot be regarded

[83] 150 F. 2d 738 (C. C. A. 3rd 1945).

[84] That the circuit court based its decision on Section 2, not Section 1, of the Sherman Act is apparent from its opening statement:

"The question we meet is whether plaintiff has supported its charge of illegal monopoly that defendants have violated Section 2 of the Sherman Act . . . in order to support an action for injunctive relief and triple damages under Section 4 of the Clayton Act. . . . Plaintiff relied too on Section 1 of the Sherman Act . . . ; and while this section states an additional offense 'the two sections overlap in the sense that a monopoly under Section 2 is a species of restraint of trade under Section 1.' " *Id.* at 740.

[85] *Id.* at 745.

[86] The court, commenting upon this evidence, said it showed that "there is concert of action in what has been done and that this concert could not possibly be sheer coincidence. We think there must have been some form of informal understanding." *Id.* at 743.

The Court then laid stress on the fact that defendants had put in no evidence at all to rebut or explain the inference of conspiracy, and cited and quoted from the *Interstate Circuit* decision on the failure of defendants in such situations to produce their responsible executive officers to testify.

as authority for the "conscious parallelism of action" doctrine, as the Federal Trade Commission would apply it to delivered pricing cases. Industry-wide use of delivered pricing has been loosely characterized by the Commission's spokesmen as a "monopolistic" practice, but this charge has proceeded from the argument that delivered pricing is the cause of price uniformity and that price uniformity is an evil in and of itself. In the *Goldman* case the result of the distributors' contracts with Warner was a true monopoly, in the traditional sense of the term, even though it applied to a limited geographical area and a limited product. Knowledge of that fact on the part of the distributors was proved, but that knowledge is far different from the mere knowledge acquired by a business man from his dealings in the trade that he is using a delivered pricing method which is the same as his competitors and that, when he meets competitors' prices, there will be price uniformity.

The *Goldman* case may stand for the proposition that a seller may not safely make a contract to sell exclusively to one buyer if he knows that all other sellers are doing likewise with a resulting monopoly in that buyer. To the extent that the *Goldman* case enters the field of implied conspiracy, however, it must be limited to its facts, including the fact of actual monopoly and the fact that (as in the *Interstate Circuit* case) the defendants refused to testify in an effort to explain away the inference of an informal understanding.

III

Present Legal Status of Doctrine

However illogical may be thought the Commission's position in adopting and advocating its "conscious parallelism of action" theory, as long as the Commission occupies its present status as a "body of experts" that theory cannot be lightly written off. The courts may be on the verge of changing the theory into a rule. That this has not yet occurred, but that latent possibilities exist is shown by examination of (1) the *Rigid Steel Conduit* case, (2) the Supreme Court opinion in the *Cement* case, (3) a series of opinions of the Seventh Circuit Court of Appeals, and (4) the *Crown Manufacturers* case.[87]

The *Rigid Steel Conduit* case shows both the trend and its non-realization. On the one hand is a cease and desist order embodying the "conscious parallelism of action" theory, and affirmance of that order by both the Seventh Circuit Court of Appeals and the Supreme Court. On the other hand, the Supreme Court affirmed merely by virtue of a four-to-four vote. Neither court produced an opinion which really upholds the "conscious parallelism of action" theory,[88] and the Commission has disclaimed the apparent effect of the case as a precedent.[89]

The Seventh Circuit Court of Appeals, in its opinion, obviously erred in basing its discussion of the Count II issues on the premise that: "In this situation, and

[87] Bond Crown & Cork Co. v. Federal Trade Comm'n, 176 F. 2d 974 (C. C. A. 4th 1949).

[89] See note 43 *supra*.

[88] There was no opinion by the Supreme Court, of course.

indeed all parties to these proceedings agree, the legal question presented is identical with the one the Supreme Court considered in the Federal Trade Commission v. Cement Institute case."[90] The *Rigid Steel Conduit* case was argued to the Circuit Court of Appeals on January 19, 1948, or several months before the *Cement* case was decided by the Supreme Court. The issues decided by the *circuit court of appeals* in the *Cement* case were (1) that the Commission failed to find a conspiracy, (2) that assuming adequate findings of a conspiracy the evidence did not support such findings, and (3) that in the absence of a conspiracy the use of the multiple basing point system by the cement industry did not constitute an unfair method of competition. It was this third issue decided by the circuit court of appeals to which the comparison was made when the *Rigid Steel Conduit* case was argued in that court. In subsequently deciding the *Cement* case, the Supreme Court held that there *were* findings of a conspiracy and that the evidence did support such findings, so that the Supreme Court, as Justice Burton's dissent points out,[91] did not reach the third issue which comprised the bulk of the lower court's opinion in the *Cement* case.

Following this misapprehension, the circuit court of appeals in the *Conduit* case quoted from the Supreme Court opinion in the *Cement* case language which probably is *dictum* and which certainly relates only to a minor collateral issue[92] in that case:[93]

> . . . individual conduct, . . . which falls short of being a Sherman Act violation may as a matter of law constitute an "unfair method of competition" prohibited by the Trade Commission Act. A major purpose of that Act . . . was to enable the Commission to restrain practices as "unfair" which, although not yet having grown into Sherman Act dimensions, would most likely do so if left unrestrained. The Commission and the courts were to determine what conduct, even though it might then be short of a Sherman Act violation, was an "unfair method of competition."

Without further discussion the Seventh Circuit Court of Appeals then concluded that it could not say the Commission was wrong in holding that the individual use of the basing point method as used in the rigid steel conduit industry constituted an unfair method of competition.

Thus the Seventh Circuit Court of Appeals did not discuss the merits or demerits of the "conscious parallelism of action" theory, but apparently adopted the view that the Commission, as a "body of experts," must be supported by the reviewing courts.

Similarly, whatever significance the Supreme Court's opinion in the *Cement* case may have in this connection lies in the broad insistence that the conclusions of the Federal Trade Commission must be accepted. There are two portions of the opinion which the Commission might cite in support of its "conscious parallelism

[90] 168 F. 2d 175, 181 (C. C. A. 7th 1948).

[91] See 333 U. S. 683, 737 (1948), dissenting opinion of Justice Burton.

[92] The question whether Cement Mfrs. Protective Ass'n v. United States, 268 U. S. 588 (1925), was controlling, or relevant, as to the issues in the instant case.

[93] 168 F. 2d 175, 181 (C. C. A. 7th 1948).

of action" theory. One is that which was seized on by the Seventh Circuit Court of Appeals in its *Rigid Steel Conduit* opinion, quoted *supra*. The other, in substance, was that the Commission was not wrong "in concluding that the delivered-price system as here used provides an effective instrument which, if left free for use of the respondents, would result in complete destruction of competition and the establishment of monopoly, in the cement industry. . . . We uphold the Commission's conclusion that the basing point delivered price system employed by respondents is an unfair trade practice which the Trade Commission may suppress."[94] This statement was followed by a footnote to the effect that existence of a combination is not an indispensable ingredient of an unfair method of competition.

Neither of these points seems, however, to be directly pertinent to the question of proof of implied conspiracy. Each seems rather to relate to possible authority of the Federal Trade Commission to prohibit entirely individual use of delivered price systems, which the Commission has disclaimed any intention of doing. However, these statements might be used by the Commission to support its contention that collective use of a delivered price system for the purpose or with the effect of "matching" prices is an unfair method of competition, although independent delivered price selling is not. The distinction between such a contention and the doctrine of "conscious parallelism of action" is, for practical purposes, non-existent. Whether conspiracy is inferred automatically from a state of facts or such state of facts is held illegal per se would seem unimportant except to metaphysicians.

In addition to the chance that the Commission may be granted power specifically to apply its "conscious parallelism of action" theory *eo nomine*, there is also some possibility that the Commission may achieve an equivalent authority indirectly by being supported in the calling of identical prices accompanied by delivered price selling a conspiracy instead of "conscious parallelism of action," as the Commission originally asserted it might do.[95] In a group of recent court decisions there is a substantial quantity of *dicta* which, in the hands of clever brief writers and careless opinion writers, might ultimately be the vehicle for importing the theory of "conscious parallelism of action" into the law by another name. These *dicta* occur in five opinions of the same court, the Seventh Circuit Court of Appeals, in five delivered pricing cases where actual conspiracy was found to exist.

The first of this series is the *Maltsters* case.[96] There the Federal Trade Commission charged and found a direct price-fixing agreement, made effective in part through use of a Chicago-plus, or single basing point, system. Although the respondents were shown to have engaged in activities which under the substantial evidence rule seemingly would have warranted affirmance of the Commission's order without regard to the use of the delivered price system, the court said:[97]

[94] 333 U. S. 683, 720-721 (1948).
[95] See page 228 *supra*.
[96] United States Maltsters Ass'n v. Federal Trade Comm'n, 152 F. 2d 161 (C. C. A. 7th 1945).
[97] *Id.* at 164.

The fact that petitioners utilized a system which enabled them to deliver malt at every point of destination at exactly the same price is a persuasive circumstance in itself. Especially is this so when it is considered that petitioners' plants are located in four different states and that the barley from which the malt is manufactured is procured from eight or nine different states.

The *Maltsters* case was followed, chronologically, by the *Milk Can* case,[98] the *Crepe Paper* case,[99] the *Rigid Steel Conduit* case[100] (that portion of the opinion dealing with Count I, the finding of a conspiracy), and the *Book Paper* case.[101] In the *Book Paper* case the Court came close to inviting the Commission to put the "conscious parallelism of action" theory into effect under a conspiracy label:[102]

The petitioners did with varying uniformity use the zoning system of price quoting, and the existence of this plan which equalizes delivered prices of competitors having widely different costs at a given destination, is strong evidence in itself of an agreement to use such plan. [Citing *Rigid Steel Conduit* and *Crepe Paper* cases.] *Moreover, a uniform participation by competitors in a particular system of doing business, where each is aware of the others' acts and where the effect is to restrain commerce, is sufficient to establish an unlawful conspiracy.* [Citing the *Goldman* case.]

It may be too much to hope that in future cases the courts will keep these quotations in their proper frame of reference. In each of those five cases there was a finding of a direct agreement to fix prices or otherwise restrain competition. There seems to have been ample evidence for the reviewing court to sustain the Commission's finding of direct conspiracy, under the substantial evidence rule, without considering the presence of the delivered price system. Therefore these cases do not deserve to (although they may) be considered as precedents for the "conscious parellelism of action" theory.

Finally, the *Crown* case[103] directly extends the implied conspiracy doctrine further than any previous case, and to a point very little short of the degree herein referred to as "conscious parallelism of action." The evidence which the Commission found to show a conspiracy to fix prices and restrain competition, and which the Fourth Circuit Court of Appeals held sufficient to sustain such finding, consisted of, in addition to use of a freight equalization system[104] and uniformity of

[98] Milk & Ice Cream Can Institute v. Federal Trade Comm'n, 152 F. 2d 478 (C. C. A. 7th 1946).

[99] Fort Howard Paper Co. v. Federal Trade Comm'n, 156 F. 2d 899 (C. C. A. 7th 1946).

[100] Triangle Conduit & Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), ***aff'd per curiam sub nom.*** Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949).

[101] Allied Paper Mills v. Federal Trade Comm'n, 168 F. 2d 600 (C. C. A. 7th 1948), ***cert. denied,*** 336 U. S. 918 (1949).

[102] *Id.* at 607. (Italics supplied.)

[103] This case arose out of a proceeding by the Commission (Docket No. 4602) against 13 manufacturers of crowns (metal caps for beer and soft drink bottles) and their trade association. The complaint and the cease and desist order charged and prohibited only a conspiracy to fix prices and restrain competition, not containing any Count II, such as in the ***Rigid Steel Conduit*** case, raising the issue of individual delivered price selling as an unfair method of competition. The trial examiner had recommended dismissal of the complaint, having felt that the evidence showed no unlawful activities on the part of either the trade association or the member companies.

[104] Each manufacturer sold f.o.b. its own factory and announced that it would "equalize freight," *i.e.*, lower its price sufficiently to compensate for the freight advantage of the competitor closest to the

prices,[105] the following: (1) Standardization through the trade association of colors and designs for "stock crowns" (crowns for soft drinks which show only the name of the drink and not the name of the bottler);[106] (2) discussion at a trade association meeting in 1928 of a standard sales contract the provisions of which, although the contract was never adopted and used, were followed in large part by the various manufacturers;[107] and (3) a series of patent license agreements between the largest manufacturer in the industry and other manufacturers, which agreements required the licensees not to sell at prices lower than those of the licensor, and in connection therewith the furnishing of price information by the licensor to the other manufacturers (this price maintenance provision of the patent licenses was eliminated prior to institution of the proceedings by the Commission).

The significance of the *Crown* case in relation to "conscious parallelism of action" is twofold:

First, it demonstrates with added emphasis the attitude of reviewing courts that the inferring by the Commission of a conspiracy must not be set aside except under the most extreme circumstances. In this case there was less substantial evidence to support the inference than in any previous delivered price case. Also, there was no evidence whatsoever that an improper purpose underlay any of the five practices relied on, and there was some evidence of a "normal business reason" for each. However, the court said, "It is argued that all this is the result of the free play of economic forces, but the Commission did not think so; and this is just the sort of question that Congress intended the Commission to decide"[108] (followed by a quotation from the *Cement* opinion).

Second, it demonstrates the power of the Commission to infer a conspiracy in virtually any industry where there is delivered price selling. Where delivered price selling is found, there is ordinarily a homogeneous or standardized product and there is ordinarily a high degree of price uniformity. These are the elements men-

customer's delivery point, if any. There was no evidence of any kind in the record of any agreement to establish or continue this method of selling, an important difference from the *Cement* case.

[105] There was some evidence in the record that crown prices had been kept down in recent years below what they otherwise might have been by pressure from bottlers of 5-cent soft drinks who desired to maintain the 5-cent selling price in the face of rising costs. The court obviously was impressed not only by the uniformity of prices among the respondents but also by the price rigidity—no change in prices from late 1938 until the closing of the record in 1947. In stressing this point the court did not mention the effect of OPA during five years of this period nor the 5-cent drink factor. Examination of the opinion as a whole leaves a doubt that absence of this price rigidity would have caused a different holding by the court.

[106] The trial examiner found that such standardization was for the convenience of bottlers and users of carbonated beverages and had nothing whatsoever to do with price fixing The findings of fact of the Commission, without reciting any evidence that the standardization program was for the purpose of price fixing, merely recite that buyers of stock crowns could not obtain any advantage in price by reason of competition among the manufacturers in the realm of design, combinations of colors or appearance, and the Commissioners inferred an understanding and combination to fix prices.

[107] The draft of the contract embodied practices in effect prior to that time, so the fact that they were thereafter followed does not indicate any change of business methods toward new and greater uniformity.

[108] 176 F. 2d 974, 981.

tioned by the court in its summarization.[109] Until now, these three circumstances in conjunction have not been generally regarded as necessarily indicating a conspiracy. Yet under this case the Federal Trade Commission seems to have discretion so to find. Here is new support for Commissioner Mason's vision of thousands of potential respondents.[110]

The implication from this group of recent cases, together with the failure of Congress to agree on any delivered price legislation during the past year, is that for the immediate future this portion of the body of antitrust law will be shaped mainly by the policy makers at the Federal Trade Commission.

It is not improbable that the Commission will jettison the phrase "conscious parallelism of action" while retaining the principle.

This change of approach is foreshadowed by numerous official statements by the Commission, and semi-official statements by members of the Commission's staff, during the year following the coining of the phrase.[111] As has been noted, the policy statement itself paves the way for substitution of the word "conspiracy." Possibly some softer sounding word such as "understanding" may come into more common use.[112] The phrase "tacit conspiracy" has been used by Mr. Corwin D. Edwards, Director of the Bureau of Industrial Economics of the Federal Trade Commission, in an exposition[113] on this subject which, as a possible guide to the current and future attitude of the Commission, deserves the most careful consideration and evaluation.

IV

Problem Created By Doctrine

Although "conscious parallelism of action" has not yet achieved the status of a legal principle, the trend in that direction has reached a point which requires general awareness of its implications. Such awareness should bring an overwhelming demand for abandonment of this theory.

Culmination of the trend toward acceptance of the "conscious parallelism of action" theory means mandatory uniform f.o.b. mill pricing just as surely as does culmination of the trend embodied in the recent series of cases[114] under the Robinson-Patman Act dealing with delivered pricing.

Anything other than uniform f.o.b. mill pricing requires that sellers in most industries have the right to adjust their prices by amounts exactly necessary to

[109] *Id.* at 979. Nor are the other two elements which are found here uncommon circumstances.

[110] *Hearings, supra* note 6, at 66-72.

[111] See note 7 *supra.*

[112] See par. 13 of Commission's findings in the *Crown* case, *supra* note 87, at 976.

[113] Edwards, *supra* note 21.

[114] Federal Trade Comm'n v. Morton Salt Co., 334 U. S. 37 (1948); Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948); Corn Products Refining Co. v. Federal Trade Comm'n, 324 U. S. 726 (1945); Federal Trade Comm'n v. A. E. Staley Mfg. Co., 324 U. S. 746 (1945); Standard Oil Co. v. Federal Trade Comm'n, 173 F. 2d 210 (C. C. A. 7th 1949); see Corn Products Refining Co., FTC Docket No. 5502 (opinion of Commissioner Mason concurring in order denying motion to dismiss complaint dated July 12, 1949).

overcome the freight advantage of competitors.[115] This may be done by what is broadly called "freight absorption" or may take some other form. Inevitably it must be systematic, and ordinarily it will result in substantial identity of ***published*** (list) prices at any particular delivery point. As a practical business matter,[116] there is no middle ground between uniform f.o.b. mill pricing and "systematically matching delivered price quotations" as that phrase is used by the Federal Trade Commission,[117] except perhaps in industries with non-homogeneous products.

Such "matching" cannot be avoided. If A Company wants to do business in the territory adjacent to B Company's plant, A Company must announce to these prospective customers (or instruct its salesmen) that it will reduce its delivered prices by the amount of B Company's freight advantage.[118] Thus A is "matching" B's prices. Nor is there anything reciprocal—in any improper sense—in this situation. B is powerless to prevent A from invading B's territory by such freight absorption, and A powerless to prevent B from doing the same thing. The only thing B could do would be to lower its f.o.b. mill price to a point which would require A to absorb so much freight as to make it unprofitable to do so. In actual situations this is ordinarily not feasible. In most, if not all, industries where delivered price methods are used, the freight between plants is a relatively small portion of the total price, or there is some other precluding circumstance, such as a constant shifting of predominant demand areas, seasonally or otherwise.

It is not necessary to debate here the economic merits of uniform f.o.b. mill selling. It is assumed that mandatory uniform f.o.b. mill pricing is not desirable as a matter of public policy. This assumption is supported by Congressional sentiment[119] displayed since the *Cement* decision.

Continuously since that opinion was announced on April 26, 1948, Congress has been wrestling with the problem of "re-legalizing" geographical competition

[115] This discussion relates, of course, to the considerable number of commodities generally referred to as homogeneous or standardized.

[116] Any doubts as to the utter impracticability of non-systematic freight absorption should be dispelled by study of the testimony of a great many witnesses from a considerable number of industries before the Trade Policies Subcommittee of the Senate Committee on Interstate and Foreign Commerce pursuant to S. Res. 241, 80th Cong., 2d Sess. (1948).

[117] The phrase derives its connotation in large part from its use in the *Rigid Steel Conduit* case. See note 40 *supra*. The Commission has consistently striven to ignore the significance of non-identity of actual off-list selling prices as contrasted to identity of published prices. It has sometimes asserted that off-list selling merely constitutes instances of failure of a conspiracy to function.

In our opinion too much emphasis has been placed on sealed bids to Government agencies. See Justice Burton's dissenting opinion in the *Cement* case, *supra* note 15, at 736 n. 8. Too little credence has been given by the Commission to contentions of respondents that they have not bid at less than published prices because of a fear that such action would lead their commercial customers to press for similar price reductions. A recent example of the validity of this position is found in a news story to the effect that lower prices bid to the Air Force on serge cloth had aroused hopes of men's clothing manufacturers that they could obtain worsted at lower prices. N. Y. Journal of Commerce, July 15, 1949, p. 13, col. 3.

[118] Any lesser reduction presumably would not enable A Company to make any sales. A greater reduction would raise a Robinson-Patman Act problem.

[119] SEN. DOC. No. 27, 81st Cong., 1st Sess. 64 (1949); H. R. REP. No. 869, 81st Cong., 1st Sess. 2 (1949).

through delivered price selling. Attention has been focused, however, on amending the Robinson-Patman Act, and no real effort has been made to deal with the equally serious problem of the "conscious parallelism of action" theory under Section 5 of the Federal Trade Commission Act.

True, S. 236[120] made a stab at tackling this problem, and S. 1008[121] also proposes an amendment of Section 5. But it is highly doubtful that either bill, if enacted, could prevent the Commission, as long as the present attitude continues, from applying the "conscious parallelism of action" theory.

Therefore, since "conscious parallelism of action" will ultimately require uniform f.o.b. mill pricing, and since mandatory uniform f.o.b. mill pricing is not desired, the crucial question is how to put an end to the "conscious parallelism of action" theory.[122] The problem is how to kill the weed itself, making sure that it does not continue to flourish under a new name.

V

THE SOLUTION OF THE PROBLEM

This problem may be dealt with by the Congress, by the courts, and by the Commission itself. Under the circumstances, positive action by all three seems called for.

A. The Congress

It would be unfortunate should the Congress be forced to deal alone with this whole problem. In addition to the practical difficulty of overcoming the uncomprehending political objections to "weakening the antitrust laws," the obstacle of legislative draftsmanship seems to be considerable.

It would be a ticklish undertaking indeed to attempt to draft legislation which would *prevent* a stubborn Commission and stubborn courts from following the lure of "conscious parallelism of action," without at the same time imposing unwarranted restrictions upon the power to find conspiracies from substantial, though circumstantial, evidence. It would not be adequate merely to provide, along the lines of S. 236, that common use of a delivered price system shall not alone be considered proof of a conspiracy, but that this fact may be considered as evidence of conspiracy in conjunction with other evidence. The effect of such a statute could too easily be avoided by more or less evidence of other common but non-conspiratorial business practices.[123]

The role of Congress probably stops at merely making clear the Congressional policy in general terms. The preamble to S. 236[124] is one way this might be done.

[120] 81st Cong., 1st Sess. (1949).

[121] 81st Cong., 1st Sess. (as passed by the Senate, 1949).

[122] Amendment of the Robinson-Patman Act to forestall mandatory f.o.b. mill pricing via that route is equally necessary, of course.

[123] See discussion of the *Crown* case, *supra*, pp. 250-252.

[124] "Section 1. In order to permit the treatment of transportation costs in interstate commerce to contribute to the promotion of competition in American industry among all sellers for the business of all

Or the policy declaration might be stronger, amounting to specific enactment of the rule of reason. The Commission and the courts, it is hoped, would apply that policy in individual case situations.

Because the trend toward "conscious parallelism of action" has gone so far in decisions of the Commission and reviewing courts, a Congressional declaration of policy is probably essential. Congress should also play a watchdog role to see that its policy is being followed. If necessary thereafter, more detailed substantive legislation should be attempted.

B. The Federal Trade Commission

The problem can best be solved by reorientation within the Federal Trade Commission. This involves several steps: (1) abandonment of the views that delivered price selling is economically bad and inherently collusive; (2) abandonment of the "conscious parallelism of action" theory; and (3) adoption of a "rule of reason" *approach* to cases involving industry-wide delivered price selling.

The phrase "rule of reason" may not be an altogether happy one in this connection but is used here for want of a better. This phrase, of course, connotes the existence of a restraint on trade or competition and the determination whether such restraint is unreasonable.[125] In delivered price cases the basic question is whether there is any restraint. As to implied conspiracies, the term "rule of reason," as here used, means requiring more proof than coincidental use of ordinary, reasonable (with reference to self-interest) business practices, looking under the surface to weigh special circumstances of the industry involved, and searching for rather than assuming the facts as to injury to the public.[126] Further, there should be

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buyers; to safeguard and secure to American workers continued employment in the areas in which they now make their homes; to promote the full development of our national resources, particularly in presently sparsely settled areas, and effectively to utilize the vast transportation systems of the United States, it is the policy of the Federal Government—

"(a) to develop a consistent and coordinated program of promoting competition, as affected by transportation costs, in interstate commerce, by the Federal Trade Commission, the Civil Aeronautics Board, the Post Office Department, and the Interstate Commerce Commission;

"(b) to foster competitive private enterprise by the treatment of transportation costs in interstate commerce so that access to distant markets may be available, when economically feasible, to any competing seller;

"(c) to encourage the Interstate Commerce Commission to continue and extend the policy of promoting regional and sectional competition by the establishment of appropriate transportation rates where required and in the best interests of the national economy;

"(d) to clarify the practice by the Federal Trade Commission which will permit all competing sellers to have access to distant markets by directing the treatment of transportation costs in interstate commerce to promote competition;

"(e) to prohibit the requiring of the sale of products at f.o.b. factory or mill prices, where buyer and seller do not choose to transact business on such terms; and

"(f) to insure to all consumers the advantages of active competition in distribution of all products."

[125] United States v. American Tobacco Co., 221 U. S. 106, 179-80 (1911).

[126] General statements by the Commissioners to the Trade Policies Subcommittee of the Senate Committee on Interstate and Foreign Commerce, created pursuant to S. Res. 241, 80th Cong., 2d Sess. (1948), appear to indicate more of such searching than is indicated by analysis of recent decisions of the Commission.

consideration of the positive, not merely the negative, effects of complying with the Commission's cease and desist orders.[127]

It has frequently been said that the courts are not equipped to make the economic determinations required in applying the rule of reason.[128] But the principal reason for the creation of the Federal Trade Commission was to have an agency so equipped. If the Commission refuses to exercise this responsibility, and applies to Section 5 cases the per se doctrines of Sherman Act cases, then consideration should be given to vesting sole jurisdiction of conspiracy cases in the district courts[129] in order to give respondents the protection of jury trial, rules of evidence, proof by preponderance of the evidence, etc.

The Federal Trade Commissioners should ponder on the words of Justice Jackson in his concurring opinion in the *Krulewitch* case.[130] These thought-provoking words apply equally to findings of a conspiracy and findings of participation by "fringe" conspirators.[131]

Our experience with conspiracy cases in the antitrust field has convinced us that unlawful collusion is not nearly so difficult to prove as is popularly supposed.[132] Few businessmen are either willing liars or adroit ones. Where collusion exists a reasonably competent trial attorney, having available the fruits of a reasonably efficient field investigation, should have no great difficulty in obtaining enough admissions by examining the businessmen involved, and their correspondence, to establish the existence of the conspiracy either by direct evidence or by circumstantial evidence so strong as to be almost the equivalent.

The present difficulty with the position of the Commission in this regard is that it wants to be able to apply the "conscious parallelism of action" theory where there is no conspiracy. The difficulty results from the fact that the Commission has been controlled by economic views inconsistent with the policies of Congress as to price leadership and competition on a geographic basis.

Hope for adoption of the "rule of reason" approach by the Commission seems to rest mainly on the views of the new Commissioners. The hope cannot be realized unless the new members of the Commission have or acquire sufficient background in the field of trade regulation to grasp the problem involved and sufficient force of personality not to be subservient to the lawyers and economists on their staff.

[127] See Clark, *The Law and Economics of Basing Points: Appraisal and Proposals*, 39 AM. ECON. REV. 430, 446-447 (1949); cf. Oppenheim, *Should the Robinson-Patman Act be Amended?* in CCH, ROBINSON-PATMAN ACT SYMPOSIUM, SECTION ON FOOD, DRUG AND COSMETIC LAW OF THE NEW YORK STATE BAR ASS'N 141 (1948).

[128] *Cf.* Federal Trade Comm'n v. Keppel & Bros., 291 U. S. 304, 314 (1934).

[129] Statement on S. 1008 submitted to the Subcommittee of Senate Judiciary Committee by Raymond S. Smethurst, Counsel for NAM, in *Hearings*, *supra* note 36, at 120.

[130] Krulewitch v. United States, 336 U. S. 440, 445 (1949).

[131] Compare the differing views in the *Cement* case, of the Supreme Court (333 U. S. at 719-720) and the Court of Appeals for the Seventh Circuit (157 F. 2d at 551-555). See also Justice Burton's dissenting opinion (333 U. S. at 736-737).

[132] See statement of John D. Clark, in *Hearings before the Subcommittee on Study of Monopoly Power of the House Judiciary Committee*, 81st Cong., 2d Sess. (1949).

C. The Courts

The Supreme Court and the United States Courts of Appeal can make their contribution by performing their function of judicial review in the real sense intended by Congress.[133] A conscientious court can, without too much difficulty, require the Commission to depend on factually supported conclusions instead of mere theories.[134]

Also, the ever-present problem of careful opinion writing is particularly aggravated in delivered price cases. The Supreme Court's *Cement* opinion has been severely criticized by various members of Congress.[135] The group of delivered price-conspiracy opinions of the Seventh Circuit Court of Appeals[136] obviously shows need for more understanding of the underlying situation.

Awareness on the part of these courts of the basic Congressional policy toward the bona fide delivered price meeting of competition, and insistence that Federal Trade Commission personnel do not substitute therefor their own theories, would relieve Congress of the difficult task of legislating specifically against "conscious parallelism of action." The problem is of such magnitude that if the Commission and the courts do not solve it in a reasonable manner, Congress must sooner or later become convinced of the necessity for substantive legislation.

[133] See the dissenting opinion of Justice Jackson in Federal Trade Comm'n v. Morton Salt Co., 334 U. S. 37, 58 (1948).

[134] The most recent example is Tag Mfrs. Institute v. Federal Trade Comm'n, 174 F. 2d 452 (C. C. A. 1st 1949).

[135] 95 Cong. Rec. 7157-7158 (May 31, 1949); *id.* at 9164, 9168 (July 6, 1949); *id.* at 9233-9234, 9237 (July 7, 1949); *id.* at 11554 (Aug. 12, 1949); H. R. REP. No. 869, 81st Cong., 1st Sess. 1 (1949); SEN. DOC. No. 27, 81st Cong., 1st Sess. 5 (1949).

[136] See notes 96-101 *supra*.

THE FANTASY OF THE PHRASE "INJURY TO COMPETITION"

William Simon*

Competition is universally regarded as indispensable in the public interest. The competitive system is so much a part of our democratic, free enterprise, form of government that no one has ever even whispered less than devotion to the theory of competition.

The prices of commodities throughout the civilized world are determined either by price fixing conspiracies, by government regulation, or *by active competition among competing sellers.* Price fixing conspiracies are all against the public interest, are opposed by the overwhelming majority of the American people, and are the prime target of the Sherman Act. The planned absence of competition requires the government to regulate the rates of public utilities. Only by prices determined through vigorous competition can government regulation of business be avoided, for if the law denies the people the benefits of active competition, the public can be protected against unreasonable prices only by government regulation. Regulation of prices is not effective without, and may be expected to be followed by, regulation of production. That is the end of the free enterprise system.

I

The Issue: Promoting Competition v. Protecting Competitors

The choice is between an economy regulated by fair, but vigorous, competition, and the ultimate government regulation of industry. The controversy is between those who believe in and support the philosophy of our basic antitrust law and those who, falsely professing admiration for the competitive system, seek to avoid the competitive effects of vigorous competition. They seek protection against competition by urging that the law require rigid pricing, thus prohibiting sellers from competing.

The antitrust laws are designed to protect the public interest against "injury to competition." The law protects competition—that is, the competitive system—and not individual competitors who are trying to avoid competition. But the rigid pricing advocates, in a psychological use of significant words, seek to treat "injury to competition" as synonymous with "injury to competitors."

The truth is that competition is incompatible with avoiding injury to competitors. In every competitive effort some competitor is always hurt. There cannot be real competition, which is nothing less than a contest between rivals for the business

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of customers, without some competitors being injured. In the economic strata in which competitors are not injured there is no competition. The law cannot prevent injury to competitors without making competition illegal.

The art of semantics has frequently been used for ulterior purposes. Hitler talked about invading the Balkans to "protect" the people of Eastern Europe. Stalin speaks of "liberating" the Baltic States, shouts admiration for "democracy," and rants opposition to "American-Imperialism." In the same manner the advocates of rigid pricing and the exponents of uniform f.o.b. mill selling speak of preserving "competition."

Humpty-Dumpty was at least more candid when he said, "When I use a word, it means just what I choose it to mean, neither more nor less."[1] Let those who seek only to protect competitors admit their hostility to vigorous competition.

II

F.T.C. PRIOR POSITION ON COMPETITIVE FREIGHT ABSORPTION

The Congress passed the Sherman Antitrust Act because it believed vigorous competition would bring consumers improved products at lower prices and thereby raise our standard of living.[2] This philosophy of the Sherman Act is diametrically opposed to the arguments made in the courts in Federal Trade Commission pricing cases.

In the *Cement Institute*,[3] *Pittsburgh-Plus*,[4] *Rigid Steel Conduit*,[5] and *Standard Oil*[6] cases the Federal Trade Commission argued for rules of law under the Federal Trade Commission and Clayton Acts which, although not always necessary to the decision of those cases, would have the practical effect of requiring uniform f.o.b. mill pricing and denying sellers the right to meet competition in good faith.

In the *Cement Institute* case the Commission argued and the Court said, in spite of the express finding by both of the presence of a conspiracy, that it was not necessary to prove a conspiracy to find a pricing practice an unfair method of competition. The Commission also argued that the Clayton Act requires sellers to have "a uniform net factory price."[7]

In its brief in the *Rigid Steel Conduit* case the Commission said that basing point pricing was illegal per se and that the knowing concurrent use of a pricing system by several sellers was an unfair method of competition.[8] The Commission describes this as "conscious parallel action."[9]

[1] LEWIS CARROLL, THROUGH THE LOOKING GLASS.

[2] ANNUAL REPORT TO THE PRESIDENT, COUNCIL OF ECONOMIC ADVISERS 15 (1948).

[3] Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948).

[4] United States Steel Corp. v. Federal Trade Comm'n, Docket No. 6798 (C. C. A. 3d 1938).

[5] Triangle Conduit & Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *aff'd per curiam sub nom.* Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949).

[6] Standard Oil Co. v. Federal Trade Comm'n, 173 F. 2d 210 (C. C. A. 7th 1949).

[7] Oral Argument on October 20, 1948, before the United States Supreme Court in *Hearings before the Subcommittee of the Committee on Interstate and Foreign Commerce on Sen. Res. 241*, 80th Cong., 2d Sess. 481 (1948).

[8] Brief for Appellee, 168 F. 2d 175 (C. C. A. 7th 1948).

[9] FTC, NOTICE TO STAFF, IN RE: COMMISSION POLICY TOWARD GEOGRAPHIC PRICING PRACTICES (Oct. 12, 1948).

The Commission argued in the *Pittsburgh-Plus* case that, even in the absence of conspiracy, freight absorption and phantom freight were each equally illegal.[10]

The Commission has filed other complaints alleging that buyers located near a seller's plant have an economic right to buy at lower prices than their more distant competitors.[11] One count of a complaint, which does not allege a conspiracy, attacks the validity of a uniform national delivered price,[12] and a count in another complaint, which does not allege a conspiracy, attacks the validity of a uniform zone price.[13]

The rules of law urged in those cases would deny sellers the right to compete in distant areas beyond the territory in which they have a freight advantage over their competitors.

III

THE PRACTICAL ECONOMICS OF PRICE COMPETITION

It is urged that prohibiting competitive freight absorption will restore "price competition," eliminate conspiracies to fix identical prices, and promote competition at the fringe of each seller's natural freight advantage territory (the benefits of which will accrue to all customers through the requirement for a uniform net factory price).[14]

Price competition is said to exist only when sellers each have different delivered prices. To accomplish this result it is urged that each seller have a uniform net factory price to all buyers. While the premise ignores entirely competition at the levels of service, quality, responsibility, and integrity, it is even fallacious to assume that competition based on price alone *requires* each seller to have different prices, for when one seller is denied the right to meet (and the Clayton Act denies him the right to beat) the lower price of his more favorably located competitor, he is denied the right to compete on the basis of price.

The Commission's theory of "conscious parallel action" is that the economic effect of identical prices achieved through a seller knowingly pricing his goods in the same manner as his competitor is the same as that of identical prices achieved through conspiracy and is hence equally illegal.[15]

When two sellers ask the same price for the same commodity it may well be the result of a conspiracy. But, it may also be the result of active competition. Identical prices *alone* prove nothing. Further inquiry is required to know whether the sellers are competing on the basis of price, or conspiring to avoid competition on the basis of price.

[10] Brief for Appellee, United States Steel Corp. v. Federal Trade Comm'n, Docket No. 6796 (C. C. A. 3d 1938).

[11] Federal Trade Comm'n v. American Iron & Steel Institute, Docket No. 5508; Federal Trade Comm'n v. Clay Sewer Pipe Ass'n, Docket No. 5484; Federal Trade Comm'n v. National Lead Co., Docket No. 5253.

[12] Federal Trade Comm'n v. Chain Institute, Docket No. 4878.

[13] Federal Trade Comm'n v. National Lead Co., Docket No. 5253.

[14] FRANK A. FETTER, THE MASQUERADE OF MONOPOLY (1931).

[15] See note 9 *supra*.

Life magazine contains the proud boast of Macy's and Saks department stores that they follow conscious parallel action in their pricing. Saks wrote: "Our staff of shoppers watches Macy's and other stores for just such price competition. Each shopper is trained to telephone in as soon as she finds any item which appears to be selling at prices lower than ours so that we can immediately mark ours down." Macy's replied that it employs "81 comparison shoppers" who make more than 35,000 shoppings a week "in order to maintain our price policies."[16]

When the price of a particular Arrow white shirt sells at precisely the same price at both Saks and Macy's—and at Gimbels and a dozen other New York department stores—there is no presumption of an absence of price competition. Such price behavior is even less suspect in the sale of a homogeneous commodity where buyers will not pay more to one seller than to another.

Conspiracies to fix identical prices are admittedly eliminated by prohibiting all identical prices. But when like prices result from vigorous competition they tend to a healthy economy. Only when those prices result from conspiracy, *and thus eliminate competition*, are they destructive of our competitive economy. We can not prohibit all competition in order to prevent some iniquitous activity which eliminates competition. To do so would be tantamount to burning down the house to get rid of the termites.

Students of economics usually point to commodity exchanges as examples of true competitive markets. A long term analysis of those markets shows that whenever there is a sharp break or a sharp rise in price on one commodity exchange, it is *immediately* followed by a similar movement on all other exchanges. A price decline in Chicago wheat will be followed, within a matter of minutes, by a similar movement on the Kansas City, Minneapolis, and all other grain markets. Analysis discloses not only parallel price movements between such markets, but a parallel price relationship between markets which rarely deviates to any appreciable extent.

Is the "conscious parallel action" in those markets year after year evidence of conspiracy? Obviously not. When wheat goes up in Chicago, the absence of a similar price movement in Minneapolis results in the buying of Minneapolis wheat for sale in Chicago. The time lag in market movements is only as long as is required for communication between those markets. The price relationship between markets is relatively constant at the freight rate between markets. The lower price is in the west where the grain is grown, and, as it moves east after harvest, higher prices prevail in that direction. When Chicago wheat sells above Kansas City wheat, in excess of the freight rate between those cities, traders buy in Kansas City and sell in Chicago.

Parallel market action in grains is a normal competitive phenomenon. Salesmen may, and frequently do, compete in the same manner. When a seller can invade a distant market and *compete* (not *conspire*) with his more favorably located competitor only by absorbing freight, he should be encouraged to do so.

[16] Jan. 3, 1949, p. 2, col. 1.

To separate competitive activity in the public interest from conspiratorial activity opposed to the public interest, is the function of the law enforcement agency. The Department of Justice, with an enviable record in the enforcement of the Sherman Act, does not seem to find any insurmountable difficulties in doing so.

The myth of competition at the fringes of each seller's monopoly area (under a required uniform net factory price) presupposes that the competing sellers are each located an equal distance from a large consuming market in which each desires to compete. But, when the fringe area is a lake, a prairie, or a mountain range, there is no competition at the fringe, or anywhere else. Each seller is thereby given a monopoly in the area in which he has a freight advantage over his competitors, with the public deprived of the benefits of competition.

Economic disruption, losses in plant investments, dislocation of industrial workers, and concentration of industry (adverse to the national defense program) would clearly result from required uniform f.o.b. mill pricing, as is shown by the Report of the Senate Interstate and Foreign Commerce Committee on Federal Trade Commission Pricing Policies.[17]

A Congressional inquiry followed the decisions of the Supreme Court in the *Cement Institute* case, and of the Seventh Circuit in the *Rigid Steel Conduit* case.

When the economic impact of required f.o.b. mill pricing was analyzed, there were virtually no supporters for the view that the producer should be required to sell his goods for a uniform price at the factory door.

Five Congressional committees, including the Patman Committee, heard a total of 160 witnesses testify on this subject.[18] Yet, only seven witnesses, four Federal Trade Commission employees, and three college professors—but not a single businessman—testified in support of the philosophy that sellers should not be permitted to absorb freight to compete in distant markets.[19]

IV

F.T.C. CURRENT POSITION ON COMPETITIVE FREIGHT ABSORPTION

When the Commission's position in the above cases was exposed to public scrutiny, the Commissioners themselves disavowed that philosophy and appeared to shift their reliance to members of their staff holding more orthodox views.[20]

[17] SEN. DOC. No. 27, 81st Cong., 1st Sess. (1949).

[18] *Hearings before Senate Committee on Interstate and Foreign Commerce on Sen. Res. 241*, 80th Cong., 2d Sess. (1948), 109 witnesses; *Hearings before Senate Committee on Interstate and Foreign Commerce on S. 236*, 81st Cong., 1st Sess. (1949), 21 witnesses; *Hearings before Senate Committee on the Judiciary on S. 1008*, 81st Cong., 1st Sess. (1949), 13 witnesses; *Hearings before House Committee on the Judiciary on S. 1008*, 81st Cong., 1st Sess. (1949), 2 witnesses; and Patman *Hearings*, "Small Business Objections to Basing Point Legislation," 15 witnesses. (This computation includes some duplication.)

[19] Walter B. Wooden (F.T.C. Attorney), Everette MacIntyre (F.T.C. Attorney), Eugene W. Burr (former F.T.C. Attorney), William S. Johnson (F.T.C. Economist), Vernon A. Mund (Professor, University of Washington), Fritz Machlup (Professor, Johns Hopkins University), and Walter Adams (Professor, Michigan State College).

[20] Statement of Commissioner E. L. Davis, in *Hearings before Committee on Interstate and Foreign Commerce on S. 236*, 81st Cong., 1st Sess. 22-31 (1949); written answers of Commissioner E. L. Davis

The Commission's view now officially reported to the Congress is that freight absorption was never illegal under the Federal Trade Commission Act, in the absence of conspiracy, and that the *Cement* and *Conduit* cases apply only to conspiracy situations.[21]

In July, 1949, the Commission, although it denied a motion to modify its order in the *Conduit* case, in effect did modify the order, for it said: "The Commission does not consider that the order in its present form prohibits the independent practice of freight absorption or selling at delivered prices by individual sellers." It appeared reluctant, however, wholly to abandon its doctrine of "conscious parallel action," for, in apparent contradiction of the above statement, it added that the order does prohibit the use of the "basing-point, delivered price system . . . when done, as stated in the order, for the purpose or with the effect of systematically matching delivered price quotations."[22]

The key words there are *"or with the effect."* The effect of meeting a competitor's price may be the same whether done by conspiracy or through vigorous competition. Thus the order seems directed, at least in part, to competitive practices individually pursued. Conceivably the Commission may justify this position on the ground that it is necessary to prohibit individual conduct, formerly carried on by conspiracy, in order to dissipate the effects of the conspiracy. The point was suggested to the Supreme Court in the *Conduit* case, but was not decided when the Court divided four to four and did not file an opinion.

The Commission's position appears, however, to continue to be confused. In the pending case against the steel industry involving freight absorption, the Commission's trial attorney, an Associate Chief Trial Counsel, entered into a settlement agreement which would permit some freight absorption. On December 5, 1949, the Commission made public the settlement agreement and a memorandum of its trial counsel urging that it be approved by the Commission. At the same time it released a memorandum from the trial counsel's superior, the Chief Trial Counsel, urging the Commission to reject the settlement. As this is written the Commission has not acted.

V

WHAT IS COMPETITION?

It has often been said that competition is worth what it costs. If we are to have competition we cannot restrict its normal effects. The effect on an individual businessman may be the same whether he is driven to bankruptcy through vigorous, but fair, competition, or through a conspiracy to drive him out of business. But only in the latter case is there any injury to competition. In the former case the

(concurred in by Commissioners Ferguson and Ayres) to questions submitted by Senator E. C. Johnson, *id.* at 268-278.

[21] *Ibid.*

[22] Rigid Steel Conduit Mfgrs., CCH TRADE REG. SERV. ¶14 (Docket No. 4452, 1949).

effect on the competitor is the incidental effect of giving the public the benefits of vigorous competition.

Since admiration for competition appears to be universal, let us inquire into its meaning. The dictionary defines it as, "endeavoring to gain what another is endeavoring to gain," "common strife," "a contest between rivals," "a match between contestants," or "the effort of two parties, acting independently to secure the custom of a third by offering the most favorable terms."[23]

Competition for business is no less a contest between rivals than a baseball game. In either contest one competitor always wins while another always loses. As long as the rules of the game are fair, and the contest is conducted according to those rules, there is a bona fide contest between rivals. In any such contest one contestant will always get hurt. To require a ball game always to end in a tie score would be to destroy any vestige of a contest. To prohibit injury to business competitors is to prohibit competition among them.[23a]

VI

THE CONFLICT BETWEEN THE PHILOSOPHY OF THE SHERMAN ACT AND RIGID PRICING

Rigidity of price is used to prove the absence of competition in cases charging a violation of the Sherman or Federal Trade Commission Acts. On the other hand, flexibility of price is almost certain to result in violation of the Robinson-Patman amendment to the Clayton Act.

Sellers may absorb freight to compete in distant markets, if they walk the narrow path between charges of conspiracy to fix prices, established through evidence of rigid prices, and charges of illegal price discrimination, established through evidence of flexible prices.

The use of circumstantial evidence is, of course, fundamental in proof of conspiracy. While mere identity of price is admissible evidence under a conspiracy charge, a finding of conspiracy has never been founded on a mere showing of identical prices.

But a businessman may, nevertheless, be found to have participated in a conspiracy without any intention to do so. The *Interstate Circuit*,[24] *American Tobacco*,[25] and *Masonite*[26] cases seem to hold that a conspiracy may be proved by evidence of adherence, over a period of time, to practices also rigidly followed by competitors, under circumstances indicating the absence of a purpose to compete. It is not necessary to show that the parties communicated with one another, if an understanding can be inferred from their conduct.

Circumstantial evidence—for example, that the seller did not adhere to any particular pricing pattern—is also admissible to disprove a charge of conspiracy. The

[23] WEBSTER'S NEW INTERNATIONAL DICTIONARY (2d ed. unabridged).

[23a] For an excellent discussion of the difference between injury to competition and injury to a competitor see Statement of House Managers accompanying Conference Report on S. 1008, filed October 13, 1949 (House Report No. 1422).

[24] Interstate Circuit, Inc. v. United States, 306 U. S. 208 (1939).

[25] American Tobacco Company v. United States, 328 U. S. 781 (1946).

[26] United States v. Masonite Corporation, 316 U. S. 265 (1942).

Commission has on occasion determined whether to file a conspiracy complaint by an arrangement with the proposed respondents for a spot check of their invoices. Rigid adherence to price lists during the selected period is considered to indicate the likelihood of a price fixing agreement. However, large scale deviations are generally regarded as disproving any price fixing conspiracy. Such a test, applied by the Circuit Court of Appeals for the First Circuit, recently resulted in a reversal of the Commission in the *Tag* case.[27]

But a flexible price structure which proves the absence of a price fixing conspiracy, may, as indicated above, lead to a charge of illegal price discrimination, for any departure from the published price list may well result in a discrimination. And where there is a discrimination, the Commission is prone to find that it "may" injure competition.

It is not surprising that the Secretary of Commerce recently told the Congress that many businessmen feel they are faced with the choice of violating the Sherman Act by charging uniform delivered prices, or violating the Patman Act by charging different prices to different customers.[28] And even the Commission's Chief Economist has publicly said that the philosophy of the Sherman Act appears to be in conflict with the philosophy of the Robinson-Patman Act.[29]

VII

IS MEETING A COMPETITOR'S PRICE IN GOOD FAITH WICKED?

Section 2(a) of the Clayton Act, as amended by the Robinson-Patman Act, makes price differences illegal when they have the specified adverse effect on competition and are not within the exemptions of the statute. Section 2(b) provides that whenever the Commission has shown a price discrimination, the seller may rebut the prima facie case thus made out by showing that he made the lower price in good faith to meet competition.

Prior to the recent decision of the Court of Appeals for the Seventh Circuit in the *Standard Oil*[30] case, it was generally assumed that an affirmative showing of good faith meeting of competition was a full defense to a charge of price discrimination. The Court there held, however, that Section 2(b) is purely procedural; that the Commission makes out a prima facie case by showing a difference in price; that a showing of good faith meeting of competition does no more than shift the burden back to the Commission; and that it can then establish illegality by showing injury to competition.

For the first time, good faith meeting of competition was there ruled out as a

[27] Tag Mfrs. Institute v. Federal Trade Comm'n, 174 F. 2d 452 (C. C. A. 1st 1949).

[28] Statement of Charles Sawyer, in *Hearings before Committee on Interstate and Foreign Commerce on S. 236*, *supra* note 20, at 5, 6.

[29] Corwin D. Edwards, F.T.C. Economist, before the Second 1948 Economic Institute, Chamber of Commerce of the United States, Dec. 9 and 10, 1948, printed transcript p. 108.

[30] Standard Oil Co. v. Federal Trade Comm'n, 173 F. 2d 210 (C. C. A. 7th 1949).

defense to a charge of price discrimination. The case is now pending on petition for certiorari to the Supreme Court.[31]

Apart from the order in that case, the record shows that the Commission is of the view that the law should permit good faith meeting of competition to be a defense to a charge of price discrimination.[32] The Department of Justice takes the position that this is in fact now the law.[33]

The *Standard Oil* case involved a price difference to tank car buyers, operating their own bulk storage facilities and delivery trucks (commonly called wholesalers), over the price to tank wagon (truck) buyers (commonly called retailers). There was no charge that Standard sold to one tank car buyer at a lower price than to any other tank car buyer, or at a price lower than such buyer could lawfully have purchased like gasoline from a competitor of Standard. Nor was there any charge that Standard sold to one tank wagon buyer at a lower price than it sold to any other tank wagon buyer.

One of Standard's tank car customers, Ned's, resold gasoline only through its own retail service stations and was a persistent price cutter. Another, Citron, in part followed that practice. The others were not price cutters. All except Ned's resold gasoline purchased from Standard both to other retail station operators and through stations owned by them. The Commission found this price cutting resulted in an injury to competition at the retail level. On this finding it was held that the foregoing difference in price constituted an illegal price discrimination.

The Circuit Court said, however:[34]

> There is substantial evidence in the record, and *we think it may be assumed to be conclusive*, to the effect that the petitioner [Standard] *made its low price* to Ned's, Citron, Wayne and Stikeman *in good faith to meet the lower price of a competitor.*

Standard's wholesale customers did not receive preferential treatment over other Detroit wholesalers. It would appear that the injury to retail gasoline dealers would not have been different had Ned's purchased its gasoline from a major supplier competitor of Standard, and, therefore, Standard's good faith meeting of competition was not the direct cause of the injury at the retail level.

Indeed, it is difficult to conceive of a situation where *competition* will be injured or lessened by a seller *in good faith* meeting the lower price of a competitor. When sellers are actually competing in good faith, how can competition be injured?

The reasoning of the *Standard Oil* decision is based on the premise, believed to be a fallacious fantasy, that injury to competition and injury to competitors are synonymous. The Court said the evidence of Standard's good faith competition "may be assumed to be conclusive," presumably because Standard's "price-cutting" wholesalers could have lawfully purchased the same product at the same or a lower

[31] Standard Oil Co. v. Federal Trade Comm'n, United States Supreme Court, October Term 1949, No. 851.

[32] See notes 34, 35, 36, 38 and 39 *infra*.

[33] See note 40 *infra*.

[34] 173 F. 2d 210, 213 (C. C. A. 7th 1949). [Italics supplied.]

price from one or more of Standard's competitors. The effect on competition at the retail level would not have been different had those "price-cutters" purchased from another supplier which could lawfully sell to them at that price because it sold only to wholesalers in that area. How can the good faith meeting of a competitive price, which competitors are lawfully offering to the seller's customers, be said to injure competition, regardless of what it does to competitors?

Retail competition was not hurt by what Standard did. Any injury resulted from the fact that Ned's, because it owned its own bulk storage plant and distribution facilities, was able to buy in tank car quantities at wholesale prices.

Standard's wholesale customers could continue to undersell the prevailing service station price by purchasing from Standard's competitors, who sell only in tank car quantities, just as others now do. Standard's difficulty arose from the fact it sold to both wholesalers and retailers in the same area, even though it sold to each class at or above the prevailing price to that class of customer.

During the oral argument of the *Standard Oil* case, the Court asked Commission counsel if a discrimination could ever be justified under Section 2(b), as there would always be some injury to someone in every discrimination. The reply was that Congress intended the defense of good faith meeting of competition to apply when the charge is injury to competition at the seller's level, but not when there is a claim of injury to competition at the buyer's level.[35]

In a complaint against General Foods Corporation there is a charge of geographic price discrimination where it is affirmatively alleged that a lower price made on the west coast was available in that area to all buyers alike, "wholesale grocers, direct buying chains, and independent retail grocers." That complaint even alleges that the seller took precautions to insure that the lower price not be available to anyone in areas where it was not available to all.[36]

Those who believe in, and whose obligation it is to promote, the competitive system, have urged that good faith meeting of competition be a full defense to a charge of price discrimination.

Let us examine the position of the Federal Trade Commission itself. Its October, 1948, "Statement of Policy" says that the Clayton Act "prohibits price discriminations which injure or prevent competition, unless either the price differences can be justified by differences in cost or else the price reductions have been made in good faith to meet the equally low prices of competitors." By way of a footnote, it apologetically added that it was seeking to "ascertain" in the pending *Standard Oil* case whether this is so where there was an injury to buyers.[37]

In February, 1949, the Commissioners advised a Senate Committee that meeting competition in good faith should be a defense to a charge of price discrimination and that "in general the policy of the law should not discourage active competition by preventing the meeting of competition in good faith."[38]

[35] Oral argument, pp. 53, 54, 173 F. 2d 210 (C. C. A. 7th 1949).
[36] General Foods Corporation, Federal Trade Comm'n Docket No. 5675 (July 7, 1949).
[37] See note 9 *supra*.
[38] *Hearings*, *supra* note 20, at 274, 275.

Less than three weeks after the *Standard Oil* decision, an official Commission spokesman told a Senate Committee that it had no objection to a permanent change in the law to make the meeting of an equally low price of a competitor in good faith a full defense in price discrimination cases.[39]

The *Congressional Record* discloses that the O'Mahoney Bill,[40] in a form clearly making good faith meeting of competition a full defense to a charge of price discrimination, was drawn by members of the Commission's staff.[41]

The strength of the Commission's view was tested when it was asked to comment on the Kefauver amendment to that bill, limiting the defense of good faith meeting of competition. This was embarrassing for the Commission because Senator Kefauver is one of its staunchest supporters. Yet on June 9, 1949, the Commission wrote the Congress that, ". . . all of the Commissioners believe that on balance it would be preferable to make the good faith meeting of competition a complete defense."[42]

The office of the Attorney General has consistently supported good faith meeting of competition as a complete defense. Shortly before the circuit court decision, the Department of Justice advised a Senate Committee that the present law "permits sellers to justify otherwise forbidden price discriminations on the ground that lower prices to one set of buyers were made in good faith to meet the prices of a competitor."[43] The Department of Justice later recommended "deletion of the parenthetical phrases in Sections 2 and 3, the so-called Kefauver Amendment. The effect of these phrases is to eliminate the defense that acts of freight absorption or price discrimination, charged to be a violation of the Clayton Act, were undertaken in good faith in meeting competition where the effect of such acts would be to substantially lessen competition."[44] After the House Judiciary Committee followed that recommendation, the bill was expressly approved by both the Attorney General and the White House.[45]

In their December, 1948 report to the President, his Council of Economic Advisers criticized the Patman Act for prohibiting business practices long regarded as legitimate features of hard rivalry for business.[46]

One of its members recently told the House Judiciary Committee that the Council of Economic Advisers had proposed corrective legislation because they felt "the law

[39] *Hearings before the Senate Committee on the Judiciary on S. 1008*, 81st Cong., 1st Sess. 72 (1949).

[40] Sec. 3 of S. 1974 (later substituted for S. 1008), 81st Cong. (1949).

[41] 95 Cong. Rec. 11491-11492 (Aug. 11, 1949).

[42] Letter dated June 9, 1949, from E. L. Davis, Acting Chairman, Federal Trade Commission, to Francis E. Walter, in *Hearings before House Committee on the Judiciary on S. 1008*, 81st Cong., 1st Sess. 61 (1949).

[43] *Hearings, supra* note 20, at 320.

[44] Testimony of Herbert A. Bergson, Assistant Attorney General in Charge of the Antitrust Division, *Hearings, supra* note 41, at 12.

[45] 95 Cong. Rec. 9164 (July 6, 1949).

[46] See note 2 *supra*.

and the Commission had stepped over the line between unfair methods and those which are the essence of vigorous competition."[47]

He asked the Congress: "Is it a desirable national policy to tie the hands of the big competitor and thereby make it easier for the small business man to survive?"

And he gave this answer:[48]

> I have no doubt that Woodrow Wilson and his predecessors would have furiously protested any such proposal. Today, many supporters of the antitrust policy will give hesitant answers. My own is that there is a heavy burden of proof upon him who would temper the storms of competition for the lamb in this manner. He must do more than argue for stability of business. He must make an exceedingly strong case that his proposal will not, by depriving competition of its vigor, deny the people those benefits of larger production, lower costs and prices, and improved standards of living which the Sherman Act was designed to promote.

Senate Bill 1008, as reported out of conference on October 13, 1949, would make lawful the good faith meeting of a competitor's equally low price, as well as competitive freight absorption, subject to the limitation that the bill not make lawful any combination, conspiracy, or unlawful agreement; or any monopolistic, deceptive, fraudulent, or oppressive practice. The House of Representatives approved the Report October 14, 1949.

VIII

THE BASIC CONFLICT INVOLVES OUR FREE ENTERPRISE SYSTEM

The conflict is between those who, while paying lip service to competition, in fact seek protection from it, and those, on the other hand, who whole-heartedly support our antitrust philosophy.

The economic issue is whether we are to deprive 145 million people of the benefits of vigorous competition in order to insure financial stability to the few who are either unable, or feel they are unable, to withstand the rigors of vigorous, but fair, competition.

A member of the Federal Trade Commission recently told a Senate Committee:[49]

> I yield to none in my desire to see a free competitive economy in the United States survive and to preserve to industry and our people the prosperity and freedom we have achieved under the capitalistic system. Free competitive enterprise is the foundation of our capitalistic system. Whatever weakens that foundation weakens the life-blood of industry and the capitalistic system. . . . *It is the duty of the Commission* to seek the interpretation of important legal points at issue and *to promote and foster competition in industry.*

Yet the Commission, which considers its *duty* to be to "promote and foster com-

[47] Testimony of John D. Clark, in *Hearings before Subcommittee on Monopoly Power of the House Committee on the Judiciary*, 81st Cong., 1st Sess. 114 (1949).

[48] *Ibid.*

[49] Commissioner E. L. Davis, in *Hearings*, *supra* note 20, at 26. (Italics supplied.)

petition," has entered an order finding illegal a competitive practice which it describes as follows:[50]

> The competitive effects of respondent's discriminatory prices on other manufacturers of controls are persuasively indicated by its own arguments that its discriminatory prices were made for the purpose of meeting competition. *These arguments show that respondent's discriminatory prices were made to retain the business of certain customers* or to secure the business of others and that they were largely successful in doing so. *To the extent that business is held by or diverted to respondent from its competitors* by its discriminatory prices and unfair practices, competition has been adversely affected within the meaning of the law.

To reach the conclusion that "competition has been adversely affected" to "the extent that business is *held* by" a seller who varies his price "*to retain the business* of certain customers," is certainly giving the word competition a meaning not found in the dictionary.

That conclusion also eliminates the good faith meeting of competition, for proof of good faith meeting of competition automatically proves a price to try to hold business, or to divert business, from a competitor. This is apparently considered by some to be proof of an adverse effect on competition.

We are here discussing *good faith* competition. The emphasis is on "*good faith.*" Predatory practices and strong arm methods to drive competitors out of business are never in good faith. Selling below cost or local price cutting in one area, offset by profits in other areas, for the purpose of driving competitors in that area out of business to gain a monopoly for the aggressor, is certainly not within the law.

Woodrow Wilson said he took off his hat to the businessman who, by selling a better product at a lower price, was able to run his competitor out of business. There are many today who would brand him a "tool of the monopolist," for such a statement.[51]

Competent, aggressive, and energetic small businessmen find they are well able to compete with their larger competitors. The financial disadvantages of smallness can be, and frequently are, more than offset by the advantages of service, friendliness, and personal contact. The independent merchant who exploits his advantages of personal supervision is tough competition for his larger competitors.

We must make a choice between soft competition and hard, vigorous competition; between promoting competition and protecting competitors; between forcing the public to pay higher prices to guarantee profits to the marginal and inefficient merchants and giving the public the benefits of competition; between prohibiting aggressive competition and protecting those who are either unwilling or unable to engage in aggressive competition. We cannot have both.

[50] Federal Trade Comm'n v. Minneapolis-Honeywell Regulator Co., Docket No. 4920, order entered Jan. 14, 1948. (Italics supplied.)

[51] See note 2 *supra*.

There is no choice if we are to maintain a democratic free enterprise system.

If we are to succeed in outlawing price fixing conspiracies and avoid government regulation of industry, we must permit the price of goods to be determined through open and vigorous competition. To say that restriction of vigorous competition is the road to statism, is to invite all sorts of epitaphs. But the Federal Trade Commission has itself described the choice as being between *competition* and *collectivism*, saying:[52]

> Either this country is going down the road to collectivism, or it must stand and fight for competition as the protector of all that is embodied in free enterprise.

And the Commission has described the relationship between democracy and the competitive system as:[53]

> The capitalist system of free initiative is not immortal, but is capable of dying and of dragging down with it the system of democratic government.

It is not possible to give the public the benefits of lower prices resulting from competition and at the same time protect merchants who are not willing to compete against the normal effects of competition.

If our free enterprise, democratic form of government is to survive, those responsible for government policy must stop paying mere lip service to the competitive theory of the Sherman Act.

[52] FTC, REPORT ON THE MERGER MOVEMENT 69 (1948). While directed at the absence of competition resulting from mergers, the remarks apply equally to the loss of competition.
[53] *Ibid.*

THE POLITICS OF BASING POINT LEGISLATION

Earl Latham*

The *Cement* case of 1948 was decided in April of that year.[1] It outlawed a more or less obvious form of price fixing by conspiracy to use a basing point system in forbidden ways. The case aroused an immediate controversy and a din of conflicting counsels was raised. Few cared or dared to attack the principal holding directly. Many said they saw in dicta a covert menace to free and independent enterprise. It was asserted that the law now required all sellers to quote prices f.o.b. mill, and that it inhibited every enterpriser from ever meeting the lower price of a competitor. By December, 1948, a former chairman of the Federal Trade Commission was moved to say of this view, that he had to agree with Mr. Bumble: "If the law supposes that, the law is a ass, a idiot."[2]

This essay concerns itself with the drive to have Congress take legislative action to "clarify" the law which was assumedly made unclear by the *Cement* case of 1948. The movement began with the creation of the Capehart Committee in the closing months of the Second Session of the Eightieth Congress, and ended in stalemate (perhaps only temporary) in the closing days of the First Session of the Eighty-first Congress. The sequence of events provides an excellent case study of the way in which public policy was formulated in a controversial and technical field where strong and weighty interests have vested.

I

Overture to the Capehart Committee

Representatives from the great steel state of Pennsylvania acted quickly after the *Cement* case of 1948. Both Representative Francis E. Walter and Senator Francis S. Myers introduced bills in the House and Senate respectively to provide a moratorium on further proceedings under the decision and to authorize an investigation of its effects.[3] Senator Capehart of Indiana, however, had also introduced a resolution to investigate the impact of the *Cement* decision on consumers and business.[4]

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[1] Federal Trade Comm'n v. Cement Institute, 333 U. S. 683 (1948).

[2] Robert Elliott Freer, *Let's Stop Kicking the Anti-Trust Laws Around*, remarks prepared for delivery before the Sales Executives Club of New York, Roosevelt Hotel, New York City, December 7, 1948. N. Y. Times, Dec. 8, 1948, p. 49, col. 2. Some currency had been given to this view by another member of the Federal Trade Commission, Lowell Mason. See remarks of Lowell B. Mason before the Boston Conference on Distribution, Boston, Mass., Oct. 26, 1948. A statement released to the press in the name of the Federal Trade Commission, however, denied that the law forbade freight absorption or prevented meeting competitor's prices. See FTC, Notice to the Staff, In Re: Commission Policy Toward Geographic Pricing Practices (October 12, 1948).

[3] H. R. 2222 and S. 1008, 81st Cong., 1st Sess. (1949); 95 Cong. Rec. 9168 (July 6, 1949).

[4] S. Res. 241, 80th Cong., 1st Sess. (1948), introduced by Senator Capehart and referred to the Senate Committee on Interstate and Foreign Commerce, 94 Cong. Rec. 6158 (May 18, 1948); reported

Since the Walter, Myers, and Capehart resolutions all provided substantially for the same thing, a conference was arranged between Walter, the majority floor leader (Halleck of Indiana), and the chairman of the House Committee on the Judiciary to clear the brief tangle. Representative Walter in the House agreed not to press his resolution in that body and withdrew in favor of the Senate hearing which had been authorized by the Capehart resolution. If the House and the Senate had run hearings on the same subject at the same time, there would undoubtedly have been a duplication of witnesses and testimony.[5]

The reaction of the steel industry to the *Cement* case was at first mixed, with opinion divided as to next steps for steel.[6] The *Cement* case had outlawed conspiratorial use of a multiple basing point system of delivered prices among cement companies. The chairman of United States Steel said that its subsidiary, Universal Atlas Cement Company, would comply with the Court's order. The big question was whether the Court's decision affected the use of basing point formulas in pricing steel. Some wanted to await the outcome of the Federal Trade Commission's case against the manufacturers of rigid steel conduit, and others wanted to press for Congressional legislation immediately, to protect the steel industry's pricing system, even though the question of its legality was then in the processes of litigation. By June, 1948, there were strong rumors that the steel industry would press for legislation to protect the basing point system in steel. It was the opinion of Senator Morse that the steel industry intended not merely to have the existing law "clarified" but to validate the basing point system in steel, whatever the meaning of the existing law.[7]

The point is of some importance because Senator Capehart repeatedly asserted that the existing law was so confused that clarification was necessary, and that businessmen should be informed by Congress that it was legal and proper for them to absorb freight in quoting prices to buyers. This was also the official theory of the O'Mahoney Bill which was introduced in the First Session of the Eighty-first Congress, and which will be discussed more fully below.[8] It is difficult, if not impossible, to ascertain with exactness the intention of the steel industry in this matter, but there is certainly a sense in which it could be argued that the trouble with the existing law was not that it was unclear, but that it was becoming painfully clear, and that the hope of practitioners of the basing point system was not to clarify the trend, but to reverse it.[9] Some supporters of the O'Mahoney Bill at least thought they were making basing point systems safe.[10]

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with amendments (SEN. REP. No. 1566) and referred to the Committee on Rules and Administration, 94 Cong. Rec. 7501 (June 4, 1948); reported back, 94 Cong. Rec. 7949 (June 10, 1948); passed Senate as amended, 94 Cong. Rec. 7949 (June 10, 1948).

[5] 95 Cong. Rec. 7949 (June 10, 1948).

[6] For a description of these events, see speech of Senator Wayne Morse of Oregon, 95 Cong. Rec. 7162-7169 (May 31, 1949).

[7] 95 Cong. Rec. 7163 (May 31, 1949).

[8] See pages 292 *ff. infra.*

[9] For a good statement of the meaning of the law, see Note, 58 YALE L. J. 426 (1949).

[10] See remarks of Representative Crawford of Michigan on the floor of the House: ". . . if the

On July 7, 1948, United States Steel abandoned the basing point system of delivered prices and changed to f.o.b. mill.[11] Although the steel industry was not required by the *Cement* case to go f.o.b.,[12] and although the steel industry was shown by one witness to have gone on an f.o.b. basis before the *Cement* case in some instances,[13] the impression became fairly widespread that the Supreme Court had forced the steel producers to require their customers to pay the freight.[14] It is interesting that although the steel industry (which was not involved) seemed to feel it necessary to go f.o.b., one of the respondents in the *Cement* case, according to its attorney, continued to sell cement priced and delivered at destination.[15] The new policy of United States Steel raised the price of steel several dollars a ton.[16] According to one of the witnesses before the House Small Business Committee in the summer of 1949, the change to f.o.b. pricing actually made the cost to the steel companies go down $1.00 a ton.[17] A professor of political economy at Johns Hopkins University termed the steel company action an "attempt to deceive the consumers

basing point system is done away with, in accordance with the decisions of the Supreme Court, then I think we will have worse conditions from the standpoint of the expansion of monopolies and the destruction of small enterprise. . . ." 95 CONG. REC. 9164-9165 (July 6, 1949). And further, "I see nothing whatsoever in the basing point system which destroys competition." *Ibid.* See also remarks of Representative Walter of Pennsylvania, in which he said that the opponents of the O'Mahoney bill are those who oppose basing point systems. *Id.* at 9168. At another place Representative Walter said that the bill did not "reestablish" the basing point system but failed to answer directly whether it prohibited basing point systems from being reestablished. *Id.* at 9169. The Department of Justice representative, testifying before the House Judiciary Committee, referred to the bill as basing point legislation without rebuke. *Hearings before Subcommittee No. 1 of the House Committee on the Judiciary on S. 1008*, 81st Cong., 1st Sess. 13 (1949) (hereinafter cited as *H. R. Hearings on S. 1008*).

[11] The Wall Street Journal quoted an unidentified manufacturer as saying, "The pressure on Congress to pass legislation making freight absorption a legal business practice probably will be terrific as a result of United States Steel's action. For a lot of steel users, it means higher prices; many toes will be pinched. Apparently steel officials felt they couldn't win their price case before the courts, so they're using this means to take it to the people." Wall Street Journal, July 8, 1949, p. 1, col. 6. *Fortune* said two months later, ". . . as a general rule business has far more to gain through placing its faith in the slow interpretation of law by the courts than in political action. The latter is apt to yield more confusion and bitterness. The former, however difficult, can give the kind of continuity that makes industrial democracy possible." Fortune, September 1948, p. 79.

[12] See Corwin Edwards, New England Council Speech, September 18, 1948: "The Commission has no authority to require businessmen to sell f.o.b. mill or to impose upon them any other specific pricing practice."

[13] Testimony of Otis Brubaker, United Steelworkers of America, CIO, in *Hearings before a Subcommittee of the Senate Committee on the Judiciary on S. 1008*, 81st Cong., 1st Sess. 20 (1949) (hereinafter cited as *Senate Hearings on S. 1008*). The Senate Small Business Committee report, "Changes in Distribution of Steel," accepted by Wherry and Martin, shows the same thing. *Hearings, supra*, at 20. See reaction of Senator Myers in *Hearings before a Subcommittee of the Senate Committee on Interstate and Foreign Commerce on S. 236*, 81st Cong., 1st Sess. 221 (1949) (hereinafter cited as *Senate Hearings on S. 236*).

[14] See the census of views taken by the National Small Business Men's Association, in *Hearings before a Subcommittee of the Senate Committee on Interstate and Foreign Commerce on S. Res. 241*, 80th Cong., 2d Sess. 30-49 (1948) (hereinafter cited as *Senate Hearings on S. Res. 241*), where some of those answering thought that the Supreme Court had specifically forced the steel industry into its action.

[15] Testimony of Edward A. Zimmerman, in *Senate Hearings on S. 236*, at 247.

[16] Testimony of Otis Brubaker, *Senate Hearings on S. 236*, at 195. Mr. Coyle estimated the increase at $9 a ton. See note 17, *infra*.

[17] Statement of David Cushman Coyle, in *Hearings before the House Select Committee on Small Business*, 81st Cong., 1st Sess. 97 (1949) (hereinafter cited as *Small Business Committee Hearings*).

by telling them that freight absorption was unlawful and that delivered prices were, therefore, necessarily higher than before."[18]

Whatever may have been the motivation behind the decision to adopt f.o.b. pricing, the effect upon the customers of steel producing companies was rapid, loud, and insistent. A clamor was raised for legislative action, which the steel companies encouraged by direct solicitation.[19] There was also evidence that dissident customers were reluctant to identify themselves because they might be disciplined by their suppliers.[20] The Washington correspondent of the *Rocky Mountain News* discovered a public relations firm that had been hired at a compensation of at least $11,000 a month and expenses to get the law amended. According to his account, a National Competitive Committee was established with local chapters, and agents were sent about the country to organize others. The firm is said to have stood ready to perform such jobs "as delivering to a client a ready-made nation-wide grass-roots organization." Of this attempt to manufacture pressure, Senator Morse said:[21]

> This lobbying effort was one of the best organized, one of the most heavily financed, and one of the most adroitly deceptive that has ever been addressed to the Congress of the United States.

II

THE CAPEHART HEARINGS

With beaters in the states flushing the thickets, witnesses winged their way to Washington where they gave testimony to the Capehart Committee.[22] The Committee officially consisted of Hawkes of New Jersey and Brewster of Maine on the Republican side, and Johnson of Colorado and McMahon of Connecticut on the Democratic side, with Capehart of Indiana as chairman. The major work of the Committee was done by the chairman and the general counsel, while the other members participated, presumably, as their busy schedules permitted. The stated purpose of the Senate resolution under which the Committee functioned was to inquire into existing legislation concerning government policy affecting the activities of the Federal Trade Commission and the Interstate Commerce Commission, and the impact of these policies as interpreted by the Supreme Court "with particular re-

[18] Statement of Professor Fritz Machlup, *id.* at 214.

[19] Speech of Senator Wayne Morse, 95 Cong. Rec. 7163 (May 31, 1949). The forms of solicitation included suggestions by salesmen to customers that Congress be asked to legalize basing point practices, statements by company officials to the press, and letters by company officials to customers urging pressure upon Congressmen. See 95 Cong. Rec. 11575 (Aug. 12, 1949) for further details about the public relations program. See also letter from Ben Moreell, President, Jones & Laughlin Steel Corporation, July 21, 1948, to shareholders and employees, announcing new pricing policy and need for action by Congress. 95 Cong. Rec. 11585 (Aug. 12, 1949). Ernest T. Weir, Chairman of the National Steel Corporation, followed a similar course. 95 Cong. Rec. 11585 (Aug. 12, 1949).

[20] 95 Cong. Rec. 7164 (May 31, 1949). A garden toolmaker was said to have made a price reduction of one per cent but feared reporting it because of the possibility of the loss of steel allocations. Even larger reductions were named by other manufacturers but fear of trade reprisals prevented them from declaring themselves. N. Y. Times, Oct. 14, 1948, p. 45, col. 2.

[21] 95 Cong. Rec. 7165 (May 31, 1949).

[22] The title of the Capehart Committee was Subcommittee of the Senate Committee on Interstate and Foreign Commerce on S. Res. 241.

lation to the basing point or freight equalization system of pricing."[23] The Committee was also to study the effect of the continuance or discontinuance of these pricing policies on the consumer and small businessman. In addition, it was charged with the duty of exploring the character and extent of industrial concentration in the United States.[24] The resolution establishing the Committee was adopted on June 12, 1948, and on July 30 the Committee resolved to concentrate its first efforts upon the impact upon the economy of the new basing point law as interpreted and administered by the Federal Trade Commission and the courts. It never did get into the character and extent of industrial concentration in the United States.

In August, 1948, the Committee appointed an advisory council to aid it in the inquiry directed by Senate Resolution 241. Under the direction of a chairman, forty-five people were invited and participated in the deliberations of the council. The council met three times and made a final report to the Committee recommending modifications in the law for the relief of the business community. A representative of the National Farmers Union, who was a member of the council and who attended all of its meetings, found it objectionable because of its composition.[25] Of the original members of the council, he said, there were three executives of the cement industry, whose case had started the entire controversy; a representative of one of the respondents in the *Glucose* cases of 1945; and three representatives of steel companies who were respondents in a Federal Trade Commission case. There were also seven representatives of customers of the cement and steel industries. Transportation was represented by a representative of the railroads, which benefit under basing point schemes. There were no representatives of the trucking industry which does not benefit under basing point schemes. No representative was known as a strong anti-monopolist, nor were there representatives from government departments or agencies concerned with the enforcement of the antitrust laws. Of the labor representatives, one was the head of the Cement Workers Union, and one (United Steelworkers) withdrew. Of the farm groups, only two were originally represented—the American Farm Bureau Federation and the National Grange. The National Farmers Union was added at the instigation of Senator Johnson of Colorado.[26] Congressman Patman of Texas repeated the observation of the National Farm Union representative that,[27]

> The inclusion of representatives of three great farm organizations can be accounted for only on the theory that their interest in the basing point problem had not been publicly

[23] STUDY OF FEDERAL TRADE COMMISSION PRICING POLICIES, INTERIM REPORT, SEN. DOC. No. 27, 81st Cong., 1st Sess. 1 (1949) (hereinafter cited as SEN. DOC. No. 27).

[24] The Chairman of the Federal Trade Commission objected that with $15,000 and a deadline of March 15, 1949, nothing like the investigation authorized by S. Res. 241 could be achieved. Statement of Robert E. Freer, Chairman, Federal Trade Commission, to a Subcommittee of the Senate Committee on Interstate and Foreign Commerce on S. Res. 241, 80th Cong., 2d Sess. 1 (June 2, 1948) (mimeographed).

[25] Statement of Angus McDonald, in *Small Business Committee Hearings*, at 75 *ff*. The Committee was also described by Otis Brubaker of the United Steelworkers as a basing point business committee, although he did not suggest that it was deliberately "stacked." *Senate Hearings on S. 236*, at 222.

[26] *Small Business Committee Hearings on S. 1008*, at 76.

[27] 95 Cong. Rec. 9162 (July 6, 1949). Cf. *Small Business Committee Hearings on S. 1008*, at 80.

expressed in recent years and that their devotion to the policies of the antitrust laws was underestimated.

None of the farm organization representatives agreed with the majority report of the advisory council.[28]

The center of the Committee's activities, however, was in the Committee itself.[29] Its stated object was to inquire into the impact of the Supreme Court's decision in the *Cement* case upon consumers and small businessmen. Even this was an impossible goal, for the time was too short for any reliable indication of effect to make itself apparent. As the friendly Senate Report on the hearing stated:[30]

Although many business witnesses appeared before the subcommittee and testified as to the harmful effects of required f.o.b. mill selling, it does appear that sufficient time has not yet elapsed to determine the actual effect on the cement, steel, and other industries in which that pricing practice has been adopted.

The inability of the Committee to obtain the information which it presumably was established to obtain did not prevent it, however, from compiling a record of some 1,400 pages, most of it representing, to use the language of the Senate Report, "conclusions of witnesses as to what would happen to their respective businesses if f.o.b. mill pricing was required of all industry."[31] Instead, therefore, of amassing testimony upon the effect of the Supreme Court decisions upon the economy, the subcommittee posed a fictitious situation (every enterpriser selling f.o.b. mill) and made a record of responses. There was no documented assertion that the existing law actually required anyone to adopt f.o.b. mill pricing.

The witnesses before the Committee represented steel customers,[32] cane and beet sugar growers and refiners whose products were sold on a delivered price basis,[33] candy and glucose manufacturers,[34] including some under complaint by the Federal Trade Commission, cement customers,[35] building materials manufacturers and dealers,[36] cement producers,[37] steel producers,[38] railroad traffic spokesmen,[39] pulp and paper producers,[40] some officials of the Department of Justice and the Federal Trade Commission,[41] spokesmen for trade associations in lumber,[42] gro-

[28] *Id.* at 63. The American Farm Bureau Federation neither approved nor disapproved the majority report. The National Grange and the National Farm Union representatives wrote minority reports.

[29] The Committee hearings were held on November 9, 10, 11, 12, 16, 17, 18, 19, 29, and 30; December 6, 7, and 8, 1948.

[30] SEN. DOC. No. 27, at 35.

[31] *Id.* at 36.

[32] *Senate Hearings on S. Res. 241*, at 255, 71, 259, 282, 285, 305, 323, 743, 786, 1075, 1236.

[33] *Id.* at 564, 581, 592, 606, 610, 641.

[34] *Id.* at 614, 625, 627, 1046.

[35] *Id.* at 647, 657, 667, 672, 676, 1235.

[36] *Id.* at 52, 55, 292, 662, 679, 683, 774.

[37] *Id.* at 776, 841, 852.

[38] *Id.* at 262; Pittsburgh Steel Co., *id.* at 505; Inland Steel Co., *id.* at 514, 526, 540, 1259.

[39] *Id.* at 896, 1188, 1198.

[40] *Id.* at 1012, 1034, 1038, 1049, 1055.

[41] *Id.* at 96, 111, 127, 142, 694, 790, 1347.

[42] *Id.* at 768.

ceries,[43] and other commodities, small business association representatives,[44] and representatives of the Army,[45] Navy,[46] and other federal agencies.[47] A scattered representation from assorted enterprises appeared,[48] and some minor public officials. Three unions were represented, one of which was a small union in the cement industry[49] and another in railroads.[50] All three were from industries representing basing point interests, or benefiting from basing point systems. None of the major unions appeared, although telegrams and statements were sent by several locals. None of the principal farm organizations appeared. Big steel and cement producers were notably absent. At one point in the hearings, Senator Capehart threatened to subpoena companies in the steel industry but the threat turned out to be a request for letters answering the question whether the steel companies would return to a freight absorption sales policy "if permitted by Congress so to do."[51] They thought they might.

One of the most interesting and important visitors was Senator Joseph O'Mahoney of Wyoming, who appeared in the company of Robert D. Pike, a spokesman for the Westvaco Chemical Company, Westvaco, Wyoming.[52] Mr. Pike testified that his firm was interested in developing trona deposits in Wyoming for the purpose of producing soda ash, and that the entire investment would amount to some $25,000,000.[53] He testified that his investment might be endangered if he did not have assurance that he would be permitted to absorb and equalize freight with any competitor any place in the United States.[54] Senator O'Mahoney had long been interested in developing this chemical industry in his state as a conscientious representative of Wyoming, and his appearance with Mr. Pike is evidence of the zeal with which the distinguished Senator concerned himself with the affairs of his constituents.

The hearing was a good show, with numerous witnesses to supply a chorus of protest under the direction and leadership of Senator Capehart. Although he repeatedly asserted that he wanted the facts about the effect upon industry of required f.o.b. pricing (which the law did not require), few were cross-examined except witnesses from the Federal Trade Commission, the Department of Justice, an economist from the University of Washington, and a small business group repre-

[43] *Id.* at 1061, 1162.
[44] *Id.* at 29, 1116, 1227, 1240.
[45] *Id.* at 85, 923.
[46] *Id.* at 928.
[47] Reconstruction Finance Corporation, *id.* at 885; Bureau of Federal Supply, *id.* at 917, 921; Agriculture, *id.* at 933.
[48] *Id.* at 64, 277, 296, 356, 534, 561, 631, 762, 875, 901, 912, 980, 996, 1079, 1159, 1172, 1210, 1221, 1254, 1261.
[49] United Cement, Lime and Gypsum Workers, *id.* at 19, 1148.
[50] Order of Railway Conductors, *id.* at 1206; Glass Bottle Blowers Association of the United States and Canada, *id.* at 971.
[51] *Id.* at 1374.
[52] *Id.* at 949.
[53] *Id.* at 955.
[54] *Ibid.*

sentative, all of whom testified either that the law didn't require f.o.b. pricing or that they thought that it would be a good idea if it did. Harmony prevailed in the relations between the subcommittee, its chairman, and all other witnesses. With the skill of a conductor on the podium, Capehart led witness after witness (once their prepared statements were out of the way) through a series of questions that made it appear that enterprisers were confused by the existing law, that they had no place to go in the government for a definitive answer, and that it was necessary for Congress to come to their rescue and write legislation on the subject. He was his own best witness, and he spoke to the record through many voices. He finally worked himself around to the view that the *Cement* case of 1948 was a boon to United States Steel,[55] the larger steel companies, and big business,[56] and that he was defending the little businessman, presumably by "forcing" the steel industry to stop f.o.b. pricing.[57] The representative from Inland Steel lent a hand to this piece of dramaturgy by saying that f.o.b. pricing would be to the advantage of the steel industry but that he opposed it because it would stifle competition and lead to monopoly.[58] One of the more imaginative speculations about the consequences of required f.o.b. pricing was Capehart's suggestion to a witness that it was injurious to health, because more people would be poisoned by "smog" created by concentrated industries—concentration being an alleged consequence of required f.o.b. pricing.[59]

In matters of substance, the Capehart hearings produced a potpourri of paradoxes and contradictions. Big business wanted new legislation but small business enterprisers argued their case for them. The normal competitive advantage of low freight cost (nearness to mills) was represented as offensive monopoly. The industry wide system of uniform delivered prices which lends itself to the curtailment of price competition under conditions of conspiracy or conscious parallelism, was called competition. It was argued that local monopolies would be produced unless a pricing system which produced national monopolies was restored. Although all producers offer the same buyer one price under some forms of the basing point delivered price system, the Federal Government was assumed to be doing the same thing when it sells stamps for three cents everywhere, even though the Federal Government is one producer charging the same price to every buyer. Little business asked the Congress to "permit" them to employ a system (freight absorption) which works to their disadvantage more often than to their advantage since, by being small, they often do not have the resources to compete in a national market. In the interest

[55] *Id.* at 341.

[56] *Id.* at 347.

[57] *Id.* at 563. See also *Senate Hearings on S. 236*, at 224, where Senator Capehart said that he thought "that the big steel industries would welcome a law making it illegal to sell on any other than f.o.b. basis." If one assumes with Senator Capehart that the FTC and the courts already required f.o.b. pricing, it would appear that the steel companies should have supported the Federal Trade Commission. The record does not indicate such support.

[58] *Senate Hearings on S. Res. 241*, at 514 *ff.*

[59] *Id.* at 510. On this point the colloquy concluded as follows: "Senator Capehart. So we might add health. Mr. Beeson. I would like to add health."

of clarity, the Capehart Committee laid the foundation for new legislation that would take years to litigate.

One jarring note in the proceedings was supplied by the persistent off-stage racket of Congressman Wright Patman of Texas, who took a disrespectful view of the entire affair. The Senator from Indiana heckled the Congressman from Texas, in absentia, when a Texas steel producer testified that he was confused by the law on pricing, that the uncertainties of the law should be cleared up, and that Congress should do the clearing.[60] Capehart and the steel man agreed that the steel man knew more about steel than Congressman Patman.[61] The Democratic National Committee made releases of some of Congressman Patman's charges that the subcommittee was a big business committee and that the hearings were a not too covert attack upon the antitrust laws. The rumor got about that the Democratic National Committee itself would make an official statement at the behest of the "high policy makers in the Democratic Party," but Senator McMahon scotched the rumor.[62] Capehart finally took official notice of the activities of Congressman Patman by inserting into the record a release bearing the heading of the Publicity Division of the National Democratic Committee.[63] The release contained the text of Congressman Patman's charges, with many citations from the press, including a *Wall Street Journal* report of an interview with a leading steel company president to the effect that a multitude of steel customers would get farther than a few big steel companies in the movement to change the law.[64] Capehart made an attack upon Patman in the hearing, charging him with making misstatements, and with being unfair. The advisory committee, he said, was not "stacked" but had been selected because of the knowledge of the members of the subject. Capehart specially mentioned the union and farm representatives. He was particularly annoyed by the Patman statement, issued after the election in November, 1948, that,[65]

> If Republicans had gained control of Congress and the Presidency, the anti-trust laws would have been repealed in 30 days and organized greed would have been in complete charge of the country.

This piece of political extravagance seemed to produce a stronger reaction than it deserved. Senator Capehart waved it in front of a subsequent witness who said appropriate and soothing things.[66]

III

THE EVOLUTION OF S. 236

The election undoubtedly had some influence upon the plans of those who wanted Congress to write new legislation on the subject of pricing policies.[67] With

[60] Statement of Ralph L. Gray, *id.* at 540-541.
[61] *Id.* at 556-557. [62] *Id.* at 1133-1134. [63] *Id.* at 1166 *ff.*
[64] *Id.* at 1167. [65] *Id.* at 1171. [66] *Id.* at 1242.
[67] See excerpt from Newsweek, November 29, 1948, reprinted in *id.* at 1257.

a change in the political complexion of the House and the Senate, the committee memberships were reshuffled and Capehart lost his chairmanship.[68] Those who assumed that the subcommittee would be making its report to a friendly and well disposed Congress were faced with a Congress of unpredictable temper. As events showed, however, the movement to write a new law went far in the new Congress and, indeed, was halted only by the tireless efforts of a small group of Senators led by Kefauver of Tennessee, Long of Louisiana, and Douglas of Illinois.

Before any report could be made to the Senate on the original Capehart Resolution (S. Res. 241), Senator Capehart, and Senator Johnson of Colorado who succeeded Capehart as chairman of the subcommittee, introduced a bill on January 5, 1949 to make permanent amendments to the Federal Trade Commission Act and the Clayton Act, as amended by the Robinson-Patman Act. The bill was referred to the Committee on Interstate and Foreign Commerce which proceeded, through the subcommittee headed by Johnson, to hold hearings.[69] At the least, this effort to secure permanent legislation before the investigating committee had reported showed haste, and justified the feeling that the sponsors were in an unseemly hurry. The bill of Senator Johnson was understood by Secretary of Commerce Sawyer to have the purpose of "preserving the existing status of regulation as businessmen generally understood it to be prior to the opinion in the Cement Case."[70] It had taken almost eleven years to get the *Cement* case decided.[71] While regulation walked with tortoise speed, relief from regulation was to fly on wings.

The proposed bill would have amended the Federal Trade Commission Act by outlawing any price fixing conspiracy or combination. This was surplusage since they were already illegal under the *Cement* case and other cases. In the absence of such agreement or conspiracy, no pricing practice was to be deemed an unfair method of competition because the delivered price was uniform on goods of like quality and grade, or was similarly uniform within any geographical zone, or absorbed freight. Practices tainted with fraud, deception, or coercion were denied the benefit of the amendment. The justifications available to a seller charged with practicing discriminatory pricing under the Robinson-Patman Act were increased. Prices lower than those of a competitor were exempted from the prohibitions of the Act where the differential was customary in the general price relationships of the respective products or "otherwise justified by the competitive situation of the

[68] Senator Johnson took over Senator Capehart's job as chairman on January 3, 1949. See *Senate Hearings on S. 236*, at 223. This did not mean a change in leadership, however, for the record shows that Senator Capehart did most of the talking on the Subcommittee side after the reshuffle.

[69] *Senate Hearings on S. 236*, at 2. The hearings were held for only three days in January and one day in February. The February meeting was held for the purpose of amending S. 236 before transferring jurisdiction over the bill to the Senate Committee on the Judiciary.

[70] *Id.* at 5.

[71] Secretary Sawyer in no way proposed that the decision in the *Cement* case as it related to conspiracy was to be modified. *Ibid.*

two or more sellers."[72] The authority of the Federal Trade Commission to require remedial action to dissipate the effects of a conspiracy was expanded.

Two people from federal agencies who had testified in the Capehart hearings appeared to testify in the brief hearings on S. 236.[73] Some new witnesses appeared to express a point of view different from the standard patter of confessed confusion, helplessness to choose acceptable pricing courses, and desire for Congressional relief.[74] Business groups, of course, were represented, among them being the Chamber of Commerce,[75] the National Canners Association,[76] National Retail Lumber Dealers Association,[77] and local and state chambers and industrial associations.[78] Counsel for food and private truck owners associations,[79] the American Bar Association,[80] and private witnesses[81] expressed the hope that Congress would do what was called for, although the witness for the truckers and the food dealers thought that Congress should be careful.[82] The chief witnesses, however, were the chairman of the Interstate Commerce Commission who wanted references to his agency stricken,[83] a group of witnesses from the Federal Trade Commission, and the research director for the United Steelworkers of America.

In the course of the questions put to the chairman of the Interstate Commerce Commission, it appeared that the questioners seemed less interested in the witness' problem than in trying to make it appear that the Interstate Commerce Commission promotes freight absorption[84] in order to encourage competition. The ICC on occasion permits blanket rates in order to allow sellers in two parts of the country to compete in the same market from which they are not equidistant. This produces a version of freight absorption in as much as the price to the consumer is not

[72] *Id.* at 3.

[73] These were Herbert A. Bergson, Assistant Attorney General, Antitrust Division of the Department of Justice, *id.* at 74, and Allen C. Phelps, lawyer and Chief of the Export Trade Division of the Federal Trade Commission, *id.* at 60.

[74] Among the new groups were the United Steelworkers of America, represented by its Research Director, Otis Brubaker, *id.* at 185, and the National Farmers Union represented by Angus MacDonald, Assistant Legislative Secretary, *id.* at 136. The National Grange appeared through J. T. Sanders, *id.* at 243.

[75] *Id.* at 168.

[76] *Id.* at 33.

[77] *Id.* at 55.

[78] *Id.* at 118, 131, 111.

[79] *Id.* at 235.

[80] *Id.* at 49. See also American Bar Association resolution in support of Congressional intervention, *id.* at 316.

[81] *Id.* at 176, 163.

[82] *Id.* at 236.

[83] He was concerned lest one of the stated policies of the bill—"to foster competitive private enterprise by the treatment of transportation costs in interstate commerce so that access to distant markets may be available, when economically feasible, to any competing seller"—be construed to alter the jurisdiction of the Interstate Commerce Commission. He felt that it would be difficult for the Commission to determine economic feasibility and that it would lay a ground for attack upon its decisions by "disappointed litigants who might charge that they were denied access to distant markets by the Commission's action." He suggested that the reference to the Interstate Commerce Commission be deleted and indicated that he thought that the basic legislation under which the ICC operates adequately provided for consideration of the element of competition in rate making. *Id.* at 7-9.

[84] *Id.* at 14-15.

the sum of the cost of production and shipping. Commissioner Mahaffie refused to say that this practice was the same as freight absorption with which the Subcommittee was concerned, in spite of insistent prodding by Senator Capehart.[85] He did express his personal view that the "prohibition of any (*i.e.*, all) absorption would be disturbing to business."[86] Capehart chose to regard this answer as an endorsement of his effort to prevent the Federal Trade Commission from requiring all sellers to adopt f.o.b. pricing, which was the theme of the Capehart hearings, but was not the law as it existed, nor the express policy of the Federal Trade Commission.

The witnesses from the Federal Trade Commission were Ewin L. Davis, Commissioner, and a group of Commission lawyers.[87] Missing from this group was Walter Wooden, Associate General Counsel of the Commission, who in the hearings on S. 241 had been subjected to a stiff cross examination by Senator Capehart and counsel for the Capehart Committee because he felt that f.o.b. pricing, although not the law, was desirable policy. The first presentation was made by Commissioner Davis, who took note of widespread misapprehensions that had followed the *Cement* case in April 1948, but thought that the misapprehension was abating.[88] He made the suggestion that Congress, by refusing to change the existing law, would do much itself to abate such confusion as might remain.[89]

Since the original drive to change the law was supposed to have been caused by the confusion among businessmen and their lawyers as to the meaning of the law and the intentions of the Federal Trade Commission, Commissioner Davis proceeded to show that the Commission had issued statements in explanation on two occasions and stood ready to issue further ones to clear up still obscure matters.[90] In its reply to the questions put by the Chamber of Commerce of the State of New York, dated January 12, 1949, the Commission had refused to say that all basing point systems were violations of the law, or to predict all of the circumstances in which conspiracy might be proved. The Commission was specific in saying that it did not advocate required f.o.b. pricing.[91] In his testimony, Commissioner Davis was equally specific in saying that a seller could absorb freight or absorb part of his manufacturing costs or any other costs in order, in good faith,

[85] *Id.* at 15-18.

[86] *Id.* at 21.

[87] Allen Phelps, Assistant Chief Trial Counsel and Chief of the Export Trade Division of the Federal Trade Commission; Robert B. Dawkins, Special Legal Assistant to the Federal Trade Commission; and Joseph E. Sheehy, Associate Director of the Bureau of Legal Investigation of the Commission.

[88] *Id.* at 23.

[89] *Ibid.*

[90] FTC, NOTICE TO THE STAFF, IN RE: COMMISSION POLICY TOWARD GEOGRAPHIC PRICING PRACTICES (Oct. 12, 1948); FTC Release, Letter from Commission to Secretary of Chamber of Commerce of State of New York, January 12, 1949. *Senate Hearings on S. 236*, at 24.

[91] Commissioner Davis was emphatic in pointing out that "The Commission has not in a single case challenged the use of the basing point method of pricing per se, separate and apart from collusion. The Commission has not challenged freight absorption per se. The Commission has not required f.o.b. mill pricing. The Commission has not challenged the legality of the use of uniform delivered prices by an individual concern." *Senate Hearings on S. 236*, at 24.

to meet an equally low price of a competitor.[92] As to the proposed legislation, he was of the view that it was neither necessary nor desirable.[93] Commissioner Davis later gave to the Subcommittee the views of a majority of the Commission on fifty-four questions dealing with Commission policy.[94] Apart from the propriety of using a public hearing to force from a quasi-judicial agency an assurance as to future policy, the Commission statement should have been sufficient clarification for all but the willfully self-confused.

Commissioner Davis commended to the attention of the Subcommittee two FTC lawyers who had been requested to appear (Sheehy and Dawkins).[95] Both expressed objections to S. 236. Dawkins echoed the view of Commissioner Davis that the rash of uncertainties was subsiding under the influence of public discussion, and that S. 236 would not reduce uncertainty but would increase it by the use of new and ambiguous concepts and words that would require long litigation.[96] Another lawyer, however (Phelps), contradicted Commissioner Davis,[97] thought that there was a drive to impose f.o.b. pricing on all sellers,[98] and felt that Congress should act.[99] The chairman of the Subcommittee thanked him for his "scholarly presentation."[100]

Differences of view expressed by the witnesses from the Federal Trade Commission, however, lent leverage to the Subcommittee in its claim of excessive uncertainty and confusion arising out of the *Cement* case. In the Interim Report to the Senate on S. 236, the contradictory statements of the FTC witnesses were laid end to end, and pronounced "confusing."[101] They were actually made to appear more confusing than they would have been, had the Subcommittee heeded the explanation made by Commissioner Davis. He later pointed out that all of the individuals had been invited in their personal capacities, that they had so testified, and then said:[102]

> The Commission regards difference of opinion among staff members and even among Commissioners as a normal incident of the development of policy and of the interpretation of law; and believing that responsible interpretations of public questions contribute to the understanding thereof, the Commission is unwilling either to require all staff members to express only its official views or to muzzle all staff members who think for themselves.[103]

[92] *Id.* at 25.
[93] *Id.* at 26.
[94] *Id.* at 268-278. These replies constituted a clear answer to legitimate questions of doubt about the policies and expectations of the Commission.
[95] *Id.* at 27.
[96] *Id.* at 97.
[97] *Id.* at 65.
[98] *Id.* at 66.
[99] *Id.* at 67.
[100] *Id.* at 69.
[101] SEN. DOC. No. 27, at 46 *ff.*
[102] *Senate Hearings on S. 236*, at 275.
[103] The reference to disagreements among the members of the Commission is documented by the record of the hearings on S. 236. On February 18, 1949, Senator Johnson wrote to Commissioner Lowell Mason, who replied March 2, 1949 that he wished to express his disagreement from the majority of the Commission on matters before the Congress. *Id.* at 337-338.

It may be said at this point that the Subcommittee under both Capehart and Johnson seemed interested in obtaining assurances that the Commission would not press the enforcement of the law rigorously in the directions which the Supreme Court had indicated were open. Capehart had previously referred to meeting with representatives of the Commission for the purpose of coming to some understanding.[104] At the time of the hearings on S. 236, however, the record did not show that such an understanding had been negotiated and much, therefore, was being made of the contradictions. Subsequently the Subcommittee took credit for producing mollifying disclaimers by the Commission and for the Commission's acceptance of the views of Commissioner Davis,[105] although even then it was still felt necessary to enact legislation to be sure that the Commission did not backslide.

One of the most thoroughly prepared presentations made to the Johnson Committee was that of Otis Brubaker, research director for the United Steelworkers of America.[106] It offered evidence, instead of speculation, that the effects of the *Cement* case allegedly feared were not taking place. Throughout the entire thirty districts of the USWA "we found not one single basic steel plant or one steel-fabricating plant which had been shut down because of the pricing change."[107] In the questioning of Brubaker after his direct statement, however, there was no effort to test the validity of his findings. Rather, Capehart undertook to swoop him off into the empyrean of speculation—to a fictitious world where the only pricing alternative is required f.o.b., to a realm "where the big steel industries would welcome a law making it illegal to sell on any other than f.o.b. basis."[108] The conclusion is permissible that the Subcommittee was more interested in proving its case than in hearing it refuted.

There was a hiatus between the third and the fourth of the four days of hearings on S. 236, a hiatus of about three weeks. In this period of time a change in strategy took place. Senators Johnson and Capehart were still pushing for permanent legislation, and Johnson instructed subcommittee counsel to revise the bill. Subcommittee counsel met with Commissioner Davis, who reportedly instructed the Federal Trade Commission staff to collaborate with subcommittee counsel in the preparation of a revised bill. Johnson approved the revision and told Commissioner Davis that he would accept the revision and try to get it through Congress "if the Commission formally approved the bill."[109] Commissioner Davis replied that the Commission opposed any legislation, and that it would not approve the bill. An amended S. 236 was nevertheless prepared. It was said by the chairman

[104] *Senate Hearings on S. Res. 241*, at 1011.

[105] SEN. Doc. No. 27, at 63.

[106] *Senate Hearings on S. 236*, at 185 *ff*. The record of the study and the testimony of the representative of the United Steelworkers was of importance in as much as it supplied some of the basis for the attack upon the movement to obtain Congressional relief which was made by Senator Wayne Morse. 95 Cong. Rec. 7162, 7164 (May 31, 1949).

[107] *Senate Hearings on S. 236*, at 202.

[108] *Id.* at 224.

[109] SEN. Doc. No. 27, at 69-70.

of the Subcommittee to have embodied the advice of Assistant Attorney General Bergson at many points.[110]

In the amended bill, the references to the Interstate Commerce Commission which were uncongenial to the chairman of that body were eliminated. Provisions of the bill would have made it harder for the Federal Trade Commission to prove any violation of the antitrust laws in the absence of conspiracy, and even the value of some of the evidence that would tend to prove conspiracy was reduced. The original aim of the bill was intact and indeed strengthened, to wit, to enact a permanent amendment to the antitrust laws on the basis of the Capehart testimony, which was largely *ex parte*, and the three days of hearings under the nominal chairmanship of Senator Johnson.

IV

THE MYERS MORATORIUM

Although S. 236 had been amended as a result of the hearings, the effort to get it adopted was abandoned[111] and support was given instead to a bill which Senator Myers of Pennsylvania had introduced before the hearings on S. 236 were finished: a bill to provide a legislative moratorium.[112] This bill, S. 1008, was referred to the Senate Committee on Interstate and Foreign Commerce, of which the Johnson-Capehart Subcommittee was a part. Under the Legislative Reorganization Act of 1946, amendments to the Federal Trade Commission Act were put under the jurisdiction of the Committee on Interstate and Foreign Commerce, while amendments to the Clayton Act were under the jurisdiction of the Committee on the Judiciary. Ten days after the hearings on S. 236, Senator Johnson introduced a resolution to transfer jurisdiction of both S. 236 and S. 1008 from the Committee on Interstate and Foreign Commerce to the Committee on the Judiciary, and this was approved by the Senate.[113]

[110] *Id.* at 64-69, *passim.*

[111] Several factors led to this change in strategy. First, the Subcommittee had failed to get Federal Trade Commission approval of the proposed legislation. This failure to approve could have lessened the chances of passage. Second, Assistant Attorney General Bergson in a speech before the New York City bar on February 17 had said that he had opposed S. 236 because it provided permanent regulation of a subject then being adjudicated, but indicated that he would not be adverse to a moratorium that would permit Congress time to develop satisfactory permanent legislation, if any should be found to be needed. *Id.* at 71. Third, it appeared that considerable time might pass before Congress would adopt S. 236, if it ever did. The chances of getting a quick moratorium that would produce the same result for a shorter time then appeared to be qutie attractive.

[112] Representative Walter of Pennsylvania introduced a similar bill in the House at the same time, H. R. 2222. In a speech to the Chicago Association of Commerce and Industry, Senator O'Mahoney said that S. 236 was abandoned because "so uncertain were the members of the committee of what the effect of that bill would be that they decided not to report it and instead to report a bill which was called the 'moratorium bill.'" 95 Cong. Rec. A4289, A4290 (June 28, 1949). The clarifiers in short were confused.

[113] S. Res. No. 76, 95 Cong. Rec. 1615 (Feb. 28, 1949). According to Senator O'Conor of Maryland, the moving spirit in the transferring of jurisdiction was Senator McCarran of Nevada. 95 Cong. Rec. 7156 (May 31, 1949).

Before any hearings were held on the Myers Bill (S. 1008), the Committee on Interstate and Foreign Commerce made an Interim Report to the Senate on the original Capehart hearings, the hearings on S. 236 as amended, and on S. 1008.[114] The Interim Report, which more nearly resembled a thesis than a report, was an argumentative attack upon the Federal Trade Commission. Attention was given to the plight of those who, under required f.o.b. pricing, would not be able to relocate their plants or build a $300,000,000 steel mill.[115] Out of pages of testimony by the United Steelworkers representative, the part which the authors of the Interim Report salvaged was a statement saying that a straight f.o.b. system was as undesirable as a straight basing point system. The same witness also said that the law did not require f.o.b. pricing, and that no legislation, therefore, was needed to allow freight absorption. On the other hand, a considerable amount of space was given to the testimony of the small number of unions who were basing point beneficiaries. There were tears for the proverbial victims of government regulation, "the small investor, widow, or orphan" who would "have unpleasant surprises with no fair warning."[116] The ambiguous surprises were evidently related to an asserted stock market decline in the securities of companies struck foul by the pricing policy which the Federal Trade Commission said it was not enforcing. Various statements of the staff of the Commission were examined for inconsistency with pedantic fidelity. Painstaking research was evident in the historical exposition of the Commission's well-known view that conspiracy is a bad thing and that basing point systems lend themselves to violations of the antitrust laws. The good faith of the Commission was challenged in the statement that,[117]

> The Commission's present disclaimer of any intention to require f.o.b. mill selling, and current confusion as to the legality of competitive freight absorption, may be examined in the light of this historical background.

Although no hearings had as yet been held on S. 1008, the hope was voiced that S. 1008 would be passed immediately by Congress[118] while further consideration was given to S. 236.

There were three days of hearings on S. 1008 at the end of March and the first of April, 1949. The bill itself was very simple.[119] The intent was disclaimed to

[114] SEN. DOC. No. 27, 81st Cong., 1st Sess. (1949).

[115] *Id.* at 21.

[116] *Id.* at 27.

[117] *Id.* at 45.

[118] *Id.* at 72.

[119] See *Senate Hearings on S. 1008*, at 1. Section 1 of the Myers bill declared "that it has not been the intent of the Congress to deprive individual companies of the right to use delivered price systems or to absorb freight to meet competition in any or all markets, provided such activities are carried on independently and in good faith, and not through any combination or conspiracy in violation of the Sherman Act as amended." Section 2 provided as follows: "Until the expiration of two years after the enactment of this Act, the Federal Trade Commission Act, as amended, and the Clayton Act, as amended, shall not be construed as depriving individual companies, in the absence of conspiracy or combination or other agreement in restraint of trade, of the right to independently use delivered price systems or to absorb freight to meet competition in any and all markets." Section 3 provided that "Nothing herein contained shall affect any proceeding pending in any Federal court of the United States on February 1, 1949."

deprive individual companies of the right, independently, to use delivered price systems or to absorb freight to meet competition in any and all markets, provided good faith was present and conspiratorial design was absent. One part of the bill provided that for two years the Federal Trade Commission Act and the Clayton Act (both as amended) should not be construed as depriving individual companies of the right, independently, to use delivered price systems or to absorb freight to meet competition in any and all markets, so long as there was no conspiracy or combination to restrain trade. The scene of action was now the Subcommittee of the Committee on the Judiciary, and the cast of characters had changed. The three members of the Subcommittee were McCarran of Nevada, O'Conor of Maryland, and Wiley of Wisconsin.

The Senate Judiciary Committee hearings on S. 1008 were notable chiefly because the CIO as an organization appeared for the first time to object to the rate and the direction in which the move to write legislation was proceeding; the Federal Trade Commission took a clear position through one spokesman; and several members of Congress also testified. The spokesman for the CIO was the research director for the United Steelworkers of America who had appeared in the hearings on S. 236.[120] He objected both to the idea of a moratorium and to the language of the proposed bill, feeling that the Supreme Court's expected decision in the *Rigid Steel* case might dispose of many points said to be controversial, and that the Myers Bill was vague enough to permit the reestablishment, entire, of the steel industry's pricing practices before the *Cement* case of 1948. He called attention to the study he had presented to the Johnson Committee,[121] felt that the Commission had settled the matters about which confusion was said to exist,[122] described how steel union locals were being solicited by steel companies to support S. 236 and S. 1008,[123] and pointed out that stockholders were being urged to write their Congressmen to the same effect.[124]

The Federal Trade Commission view was represented by the Associate General Counsel who had testified before the Johnson Committee on S. 236.[125] The views he expressed were those of the Commission, with one dissent.[126] The dissent was included in the record in the form of a communication to Senator Johnson.[127] The Commission view in brief was that the adoption of the moratorium would increase any confusion that might exist as to the meaning and application of the Federal Trade Commission and Clayton Acts.[128] Although specific weaknesses of S. 1008 might be cured by amendment and revision, the Commission's objection went to the very idea of the moratorium itself, since any such moratorium would inevitably

[120] Otis Brubaker, *Senate Hearings on S. 1008*, at 19 *ff.*
[121] *Id.* at 21.
[122] *Id.* at 25.
[123] *Id.* at 32.
[124] *Id.* at 34.
[125] Robert B. Dawkins, *id.* at 69-82.
[126] *Id.* at 69.
[127] *Id.* at 82.
[128] *Id.* at 69.

create a basis for further and additional uncertainties.[129] The Commission witness also felt that the Supreme Court might in the *Rigid Steel Conduit* case then pending clear up many matters about which uncertainty had been expressed.

The members of Congress who testified were Senators Myers and Johnson, and Representative Walter of Pennsylvania. Senator Myers of Pennsylvania, like the Commission and CIO witnesses, indicated that he was looking forward to the Supreme Court's decision in the *Rigid Steel* case before considering permanent legislation.[130] The Myers moratorium had been proposed, said the Senator, because the Johnson Bill (S. 236) dealt with a matter too complex for the Congress to dispose of in speedy fashion.[131] Although the Myers Bill suggested a two year moratorium, he was not insistent on this term.[132] Senator Johnson of Colorado took a short time to bring the record of alleged Commission inconsistencies up to date, including witnesses as recently as the day before, in the mood and the manner of the Interim Report which bore his name.[133] His most original contribution was a classification which divided those who want to encourage competition, and those who want no competition, with the Federal Trade Commission and the Supreme Court in the second category.[134] Representative Walter of Pennsylvania supported the proposed bill since he had introduced one like it in the House.[135] There were other witnesses, some of whom had appeared before the Capehart and Johnson Committees.[136] One of them, at least, seemed to have got into the wrong hearing because he wanted to talk about advertising allowances as they affected dress manufacturers, and thought that since moratoriums were in order, one might be fashioned for his problems. He indicated that he would settle for advisory opinions by the Federal Trade Commission "or somebody."[137]

V

". . . GEOGRAPHY COUNTS A LOT IN POLITICS"[138]

On April 27, the Myers Bill was reported favorably to the Senate, with an amendment.[139] The moratorium period was fixed by date (July 1, 1950), and there were changes in language designed to restrict the operation of the moratorium to

[129] *Id.* at 71.
[130] *Id.* at 5.
[131] *Ibid.*
[132] *Id.* at 7.
[133] *Id.* at 85-89.
[134] *Id.* at 86.
[135] *Id.* at 8.
[136] See, for example, George Burger, National Federation of Small Business, *id.* at 45; Angus MacDonald, National Farmers Union, *id.* at 59. See also American Steel Warehouse Association, *id.* at 95; Order of Railway Conductors, *id.* at 82; General Counsel Senate Subcommittee on Trade Policies, *id.* at 89.
[137] *Id.* at 14.
[138] Senator Wiley, *id.* at 79.
[139] SEN. REP. No. 305, 81st Cong., 1st Sess. (1949), 95 Cong. Rec. 5186 (April 27, 1949). Even as amended, the bill was regarded by the Federal Trade Commission as neither necessary nor desirable. See letter from the Commission to Congressman Patman of Texas. 95 Cong. Rec. A3524-A3527 (May 31, 1949).

the practice of freight absorption, without giving countenance to the systematic use of basing point pricing. For example, the phrase "quote and sell at delivered prices" replaced "use delivered price systems." An appendix to the bill contained a brief citation of Supreme Court cases tending to uphold the constitutionality of legislative overriders of Supreme Court cases, and it was the judgment of the Committee on the Judiciary, speaking through Senator O'Conor, that S. 1008 was within the constitutional authority of Congress to enact. There was, however, no statement as to the Supreme Court decisions which S. 1008 was setting aside. Senator Langer of North Dakota dissented from the Committee report and recommendation,[140] because the bill introduced at least four new terms and phrases in the antitrust laws without defining them.[141] It would, he said, have the practical effect of immunizing various monopolistic practices which the supporters of the bill would condemn; it would vitiate enforcement of the antitrust laws by substituting intent for practical effect as a test of violation; and it would legalize basing point systems and phantom freight through the uses that can be made of freight absorption. Senator Langer concluded that Congress was invading the sphere of the judiciary, and recommended that Congress either refuse to pass the bill, or amend it further to protect the antitrust laws.[142] His dissent from the majority report of the Senate Committee on the Judiciary laid the foundation for a strong attack upon the bill when it came up for debate.

It came up for debate on May 31 when Senator Myers moved its consideration.[143] Those who might have been opponents of the legislation, those who might have argued that Congress should let the Supreme Court work out the clarification of any possible confusion, were disarmed by the Court itself. One hour after the Senate Judiciary Committee had voted 7-2 to report the Myers Bill favorably to the Senate, the Supreme Court handed down its decision in the *Rigid Steel* case.[144] The Court had split four to four.[145] A half hour before the Myers Bill was to come up for debate Senator O'Mahoney of Wyoming talked with Myers and others about a substitute bill that he wanted to introduce in place of the one that the Committee on the Judiciary had worked on.[146] An arrangement was made to permit O'Mahoney to discuss his proposed substitute before final vote on the Myers Bill. Senator O'Conor assumed charge of the Myers Bill, and the Senate proceeded

[140] SEN. REP. No. 305, pt. 2, 81st Cong., 1st Sess. 5 (1949).

[141] These were "engaging in competition"; "absorb freight"; "in any and all markets"; and "delivered prices."

[142] See note 140 *supra.*

[143] 95 Cong. Rec. 7155 (May 31, 1949).

[144] *Id.* at 7159. Triangle Conduit & Cable Co. v. Federal Trade Comm'n, 168 F. 2d 175 (C. C. A. 7th 1948), *aff'd per curiam sub nom*, Clayton Mark & Co. v. Federal Trade Comm'n, 336 U. S. 956 (1949).

[145] "Perhaps as a result of this split decision sentiments in the Senate in favor of permanent legislation in preference to a moratorium appears to have strengthened." Testimony of Herbert A. Bergson, Assistant Attorney General, in *H. R. Hearings on S. 1008*, at 11.

[146] This was S. 1974, which was referred to the Committee on the Judiciary. 95 Cong. Rec. 7137 (May 31, 1949).

to consider the measure which was now moot because of the expected O'Mahoney substitution.

O'Conor's opening statement in explanation of the bill described the principal features of the measure. He was not accurate in making a strong implication that mere freight absorption as such was unlawful, or that the only pricing alternative available to businessmen under the law was f.o.b. pricing.[147] There was widespread confusion, he said; the expected "clarification" by the Supreme Court in the *Rigid Steel* case had not materialized; and it was now even more necessary than ever for Congress to intervene. The intervention prescribed by S. 1008 was a moratorium until July 1, 1950, on all proceedings against pricing practices except those where conspiracy or combination was involved. There was to be no permanent change in the law, and Congress was not committing itself to any particular course of action or policy after the expiration of the moratorium. He made a point of saying that the bill was not a "big business" bill but one that involved the entire economy.[148] Following the explanation, Senator Langer of North Dakota launched an attack on the bill, in the main following the points that he had raised in his dissent from the Senate Judiciary Committee Report on S. 1008, but adding new matter of a general nature, in a text full of personal reminiscences.[149]

The principal attack in this opening phase of the debate on S. 1008 was made by Senator Wayne Morse of Oregon.[150] He described the cross-pull and interplay of pressures working upon Congress, master-minded, he asserted, by the steel companies. The steel decision to go to f.o.b. pricing was not forced by the *Cement* case because, as the Small Business Committee had reported in 1948 before the *Cement* case, there had been a steady withdrawal of steel away from those markets where freight was absorbed.[151] The *Cement* case provided a pretext to the steel companies to get rid of costly freight absorption in a sellers market, he said, and shift the blame for the change to the Federal Trade Commission. Moreover, this maneuver transformed steel buyers into an "army of zealous supporters of the modification of the law which the steel industry desired."[152] He charged deliberate misrepresentation of the Federal Trade Commission's position on these matters and denied that the record showed any ambition on the part of the Commission to force enterprises to adopt f.o.b. pricing. He cited evidence to show that on June 2, 1948, at the outset of the controversy, and in January, 1949, the position of the Federal Trade Commission had been clear that the *Cement* case did not outlaw all delivered prices or require only f.o.b. prices.[153] He asserted that the propaganda line in favor

[147] See 95 Cong. Rec. 7158 (May 31, 1949), where Senator O'Conor used language that made it appear that the Federal Trade Commission felt that the *Cement* case made freight absorption unlawful. He did not cite the express denial of this made by Commissioner Davis and referred to above.

[148] *Id.* at 7159.

[149] *Id.* at 7160 *ff.*

[150] *Id.* at 7162-7169.

[151] *Id.* at 7164.

[152] *Ibid.*

[153] See p. 283 *supra.*

of revision of the laws was perfected in the summer of 1948. The offensive phrase "basing point" was discarded and the pricing practices of the steel industry were represented as being no more than absorption of freight where necessary in order to meet competition.[154] It was his conclusion, as it had been that of Senator Langer, that the blanket authorization in S. 1008 to absorb freight for the sake of quoting identical prices would legalize the entire mechanism of the basing point system.[155] Langer had begun his speech on May 31. He yielded to Morse so that the latter could get his speech in before he made a train. Langer resumed his remarks the next day, finishing his attack upon S. 1008 as sponsored by Myers. But the attack on the Myers Bill was flogging a dead horse, for it was now evident that agreement was going to settle on the O'Mahoney substitute, and Langer accepted the substitute.[156]

The O'Mahoney Bill (S. 1974) had been referred to the Committee on the Judiciary when it was introduced on May 31. The next morning, O'Mahoney met with members of the Committee on the Judiciary and discussed his bill with them, making some changes in it which he had not had time to incorporate in the text by the time he arose on June 1 to describe his bill. The clerk of the Senate made a notation of the changes as he described them. It was written in a hurry. It was proffered to the Senate without hearings. The Myers Bill provided for a short moratorium; O'Mahoney proposed moratorium forever. His substitute was a permanent revision of the antitrust laws so as "to declare that delivered prices and freight absorption are not unlawful per se."[157] The champion of the antitrust laws thus appeared as a champion of permanent amendment to the antitrust laws of a kind that even the sponsors of S. Res. 241 and S. 236 had not dared to propose.

There have been various explanations of O'Mahoney's maneuver. One of the most favorable interpretations is the suggestion that O'Mahoney figured that Congress was in a mood to enact a serious renunciation of antitrust policy. In order to avoid a more serious rout, he "preferred a strategic retreat in the form of a compromise with the forces of monopoly."[158] Against this view, perhaps, is the fact that the authors of S. 236 did not think that they could get their bill through, and that the Myers Bill which the O'Mahoney Bill replaced was more moderate than the O'Mahoney Bill, at least to the extent of being temporary and not permanent legislation. A sterner critic suggested that O'Mahoney had "become a convert to a different school of economic thought" from that he expressed as head of the

[154] 95 Cong. Rec. 7168 (May 31, 1949).

[155] Senator Myers showed himself to be concerned over some of the implications of the Morse exposition of the activities of pressure groups. At the end of the Morse speech, Senator Myers wanted his "friend from Oregon" to understand that no steel companies or any others came to Myers while the bill was being prepared. 95 Cong. Rec. 7169 (May 31, 1949).

[156] *Id.* at 7190 (June 1, 1949).

[157] *Id.* at 7204. The other of the two objectives of the bill was to "preserve the strength of the antitrust laws."

[158] Letter to Congressman Wright Patman from Dr. Fritz Machlup, Johns Hopkins University, July 6, 1949, *Small Business Committee Hearings on S. 1008*, at 212.

Temporary National Economic Committee.[159] The most candid testimony as to what O'Mahoney had in mind is the testimony of Senator O'Mahoney. On the floor of the Senate, O'Mahoney said,[160]

I should like to say to the Senator (Kefauver) that one of the purposes which I entertained in offering this provision was to make sure that the system which has been used, without criticism, by the sugar beet industry, of selling at delivered prices by absorbing freight, should not now be disturbed.

His faithfulness to his mission as a Senator with important state economic interests to promote is evident in his further statement,[161]

I wanted to be sure that that great western industry was not being unduly affected by the decision.

In the course of testimony he gave to the House Judiciary Committee in support of his bill, Senator O'Mahoney also referred to the development of trona deposits in Wyoming through the Westvaco Company, whose representative he had accompanied to the Capehart hearings. O'Mahoney at that time said that he proposed his bill to clear up the law because he felt "it was essential that nothing be done to prevent the investment of private capital in new industry in the United States."[162] He had told the Westvaco Company representatives that he thought the law did not compel f.o.b. pricing and that (absent conspiracy) the company could sell its product in the market of any other company at a delivered price and absorb freight in doing so. But no lawyer would advise the company so. O'Mahoney cited the four to four split of the Supreme Court in the *Rigid Steel* case and indicated that after that case it seemed clear to him "that we were erecting a barrier to the investment of private capital in the development of our natural resources and in the development of trade and commerce."[163] Beets and chemicals were clearly in the mind of the sponsor of the substitute for the Myers Bill, whatever other aims might have existed.

The Senate was patently confused, as the record shows. Some, like Senator Tobey of New Hampshire, had come well prepared to fight against S. 1008 in the Myers version, on the ground that it would legalize or tend to legalize basing point systems and make the problem of proof of violation of the statutes more difficult for the Federal Trade Commission, or that lawyers might so argue and thereby produce more eventual confusion than clarification.[164] Tobey felt that he was vot-

[159] Testimony of Walter Wooden, Associate General Counsel, Federal Trade Commission, *Small Business Committee Hearings on S. 1008*, at 68. See Senator O'Mahoney's speech before the Chicago Association of Commerce and Industry, June 22, 1949, as an example of the asserted conversion. 95 Cong. Rec. A4289 (June 28, 1949).

[160] 95 Cong. Rec. 7211 (June 1, 1949).

[161] *Ibid.*

[162] *H. R. Hearings on S. 1008*, at 4.

[163] *Ibid.*

[164] See the long statement inserted in the Congressional Record by Senator Tobey, 95 Cong. Rec. 7211-7231 (June 1, 1949).

ing for something different in the O'Mahoney substitute for the Myers Bill.[165] But Senator O'Conor of Maryland, who was in charge of the Myers Bill, felt that there was no substantial difference between the two except that the O'Mahoney proposal would have made permanent what O'Conor and Myers had only dared to hope to make temporary.[166] Senator Myers thought that there was no difference either. As he said:[167]

When I introduced Senate Bill 1008, in the nature of a moratorium, in the nature of temporary legislation, I was hopeful that at least we might get that much action. However at that time I did not believe that it would be possible to get permanent legislation through the Senate. However with the assistance and guidance of the Senator from Wyoming, we are able to make permanent what we originally sought to make temporary. I congratulate him for his efforts.

The Senate by a voice vote and with no real debate adopted the O'Mahoney Bill as a substitute for the Myers Bill and then passed it, not as S. 1974, but as S. 1008.[168]

[165] "Therefore I wish to go on record as saying that I am opposed to the bill [*i.e.*, the Myers Bill] itself. I shall vote for the O'Mahoney amendment in the nature of a substitute." 95 Cong. Rec. 7211 (June 1, 1949).

[166] "We feel that the amendment as proposed by the Senator from Wyoming accomplishes exactly what was intended to have been accomplished by the Committee on the Judiciary on a temporary basis, but now is accomplished on a permanent basis by the suggestion of the Senator from Wyoming, as amended in the several respects to which explanation has been given. *Id.* at 7231.

[167] *Id.* at 7232.

[168] As it passed the Senate, S. 1008 in Section 1 provided: "It shall not be an unfair method of competition or an unfair or deceptive act or practice for a seller, acting independently, to quote or sell at delivered prices or to absorb freight: Provided, That this shall not make lawful any combination, conspiracy, or collusive agreement; or any monopolistic, oppressive, deceptive, or fraudulent practice, carried out by or involving the use of delivered prices or freight absorption." *Ibid.* The Clayton Act as amended was further amended by adding that it "shall not be an unlawful discrimination in price for a seller, acting independently" to quote and sell at delivered prices, identical at different delivery points "or if differences between such prices are not such that their effect upon competition may be that prohibited by this section." Similarly, it was not to be an unlawful discrimination in price for a seller, acting independently, "to absorb freight to meet the equally low price of a competitor in good faith (except where the effect of such absorption of freight will be to substantially lessen competition), and this may include the maintenance, above or below the price of such competitor, of a differential in price which such seller customarily maintains." The parenthetical phrase is the Kefauver amendment referred to below, *infra*, note 171. Section 2(b) of the Clayton Act as amended was further amended to read: "Upon proof being made, at any hearing on a complaint under this section, that there has been discrimination in price the effect of which upon competition may be that prohibited by the preceding subsection, or discrimination in services or facilities furnished, the burden of showing justification shall be upon the person charged with a violation of this section, and unless justification shall be affirmatively shown, the Commission is authorized to issue an order terminating the discrimination: Provided further, That a seller may justify a discrimination (other than a discrimination which will substantially lessen competition) by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor." The parenthetical phrase is also a Kefauver amendment. Both amendments were designed to retain the rule of the Seventh Circuit Court of Appeals in Standard Oil Co. v. Federal Trade Comm'n, 173 F. 2d 210 (1949), where the effect of price discrimination on competition was held to overcome the defense of good faith. 95 Cong. Rec. 7211 (June 1, 1949). At one place, Senator O'Mahoney told Kefauver that he did not think that his bill (before the Kefauver amendment) would "change the ruling under which the Federal Trade Commission now operates" but he later admitted that the effect of his language would be adverse to the rule in the *Standard Oil* case (Standard Oil Co. v. Federal Trade Comm'n, 173 F. 2d 210 (C. C. A. 7th 1949)). 95 Cong. Rec. 7206 (June 1, 1949). The fourth section of S. 1008 contained definitions, one of which was: "The term 'effect may be' shall mean that there is substantial and probative evidence of the specified effect."

There had been no hearings on it. Some of the Senators obviously did not understand what was happening. O'Mahoney gave only a very general kind of explanation. In fact, some of the provisions were fashioned by question and answer. It seems not to have been in existence forty-eight hours previously.[169] It accomplished overnight what Capehart and Johnson stopped trying to accomplish after a long struggle of almost a year. The reputation of the Senator from Wyoming as a champion of the antitrust laws seems to have been accepted as a guarantee of his proposal.[170] Only Senator Kefauver of Tennessee and Senator Long of Louisiana showed signs of doubt. Kefauver got O'Mahoney to accept an amendment that would have refused legal countenance to freight absorption which "will substantially lessen competition."[171] The effect of this amendment was to weaken the defense of good faith, and to restore the rule of the Robinson-Patman Act that discriminatory prices were unlawful (good faith or not) where they could not be justified by cost differentials and tended to lessen competition. After the vote, Senator Long said that he was inclined to feel "that when everyone is as happy about a piece of legislation as Senators appear to be, someone is going to be fooled when he wakes up and sees what is in it."[172] A subsequent motion on June 6 to reconsider the bill was defeated,[173] and on that day the O'Mahoney version of S. 1008 was referred to the House Committee on the Judiciary.[174]

VI

FROM HOUSE TO HOUSE

The bill which was given no hearings at all before it was proposed to and passed by the Senate, was given no hearings to speak of in the House. According to one witness, the Judiciary Committee announced a one-day hearing which he heard about "by the grapevine."[175] One accomplishment of the one-day hearing was to prune the bill of the amendment that Senator Kefauver had had inserted. Although he accepted the amendment on the floor of the Senate,[176] Senator O'Mahoney appeared a week later at the House Judiciary Committee hearings to propose that it be taken

This would have reversed the rule of Federal Trade Comm'n v. Morton Salt Co., 334 U. S. 37 (1948), where it was held that a "reasonable possibility" of injury to competition could make a price discrimination unlawful. See also Corn Products Co. v. Federal Trade Comm'n, 324 U. S. 726, 742 (1945).

[169] Congressman Walter said that the bill as it passed the Senate had been drafted by Assistant Attorney General Bergson. 95 Cong. Rec. 9158 (July 6, 1949). At another time Senator Johnson of Colorado said that the Federal Trade Commission was the source of the bill. 95 Cong. Rec. 11491 (Aug. 11, 1949), and that Robert Dawkins was the author. *Id.* at 11492.

[170] See the comments of Senator Lucas of Illinois and Senator Myers of Pennsylvania to this effect. 95 Cong. Rec. 7232-7233 (June 1, 1949).

[171] *Id.* at 7211. The verb "will" was to be important. See *infra*, note 236, and pages 305-308.

[172] *Id.* at 7132. Note that Senator Long was also in doubt and confusion as to what was taking place. He said that even though he was in favor of the O'Mahoney amendment, on the voice vote, he voted against the bill. He thought that the amendment improved the bill, a remark that is difficult to comprehend.

[173] 95 Cong. Rec. 7391-7392 (June 6, 1949).

[174] *Id.* at 7457.

[175] Angus McDonald, National Farmers Union, in *Small Business Committee Hearings on S. 1008*, at 84.

[176] 95 Cong. Rec. 7211 (June 1, 1949).

out.[177] Herbert Bergson of the Department of Justice also appeared and suggested that the Kefauver amendment be removed.[178] While the foes of monopoly were thus engaged in building up the defenses available to respondents charged with lessening competition, Congressman Walter announced that the Federal Trade Commission had authorized him to state that the Commission was not opposed to the legislation,[179] although it had been opposed to the lesser regulation first proposed by Senator Myers. It is perhaps a tribute to the leadership of O'Mahoney that he had been able to join the Department of Justice, the Federal Trade Commission, Senators Myers, O'Conor, Capehart, Johnson, and McCarran, and Congressman Walter in a consensus for his bill. Because of the weight of this influence and the speed with which the measure moved through legislative channels without adequate hearings, the critics of the O'Mahoney Bill could fight only a rearguard action.[180] This they did in brilliant fashion, first in the House and then in the Senate. They were caught unawares when O'Mahoney's substitute passed the Senate, but they fought literally from house to house, and won at the least a temporary stalemate when the Senate failed to act on the conference version of the O'Mahoney Bill at the end of the First Session of the Eighty-first Congress.

The first attack took place in the House Judiciary Committee. Although it was evidently originally intended that the Subcommittee would hold hearings of only one day to hear O'Mahoney and Bergson, opportunity was provided to Congressman Wright Patman to make a statement.[181] The occasion was the meeting of the full Committee on the Judiciary under the chairmanship of Congressman Celler of New York to decide what action it would take on S. 1008. Before it went into executive session on June 14 to decide to report the bill favorably, Patman and three other Congressmen were heard. He urged the Committee to hold a complete and full hearing because the bill, in his opinion, would "put a loophole in the antitrust laws that a B-36 could fly through."[182] There was no other argument he could make since the Subcommittee had already reported to the full Committee, and the discussion of the merits was presumably foreclosed. There had never been, of course, any public discussion anywhere on the merits. Congressman Jennings

[177] *H. R. Hearings on S. 1008*, at 9. A later discussion showed that the printed version of the Kefauver amendment was not in the form the author intended. It had passed in a form more restrictive of the Federal Trade Commission than he had at first thought. See 95 Cong. Rec. 11477 (Aug. 11, 1949).

[178] *H. R. Hearings on S. 1008*, at 12.

[179] *Id.* at 6, 28. In an ambiguous statement, the Commission seemed to imply that the Kefauver amendment needed to be eliminated or modified in order to make good faith meeting of the lower prices of a competitor a complete defense to a charge of unlawful discrimination, although it did not make elimination of the Kefauver amendment a condition of approval. See reference to a caucus between Congressman Walter and Commission Staff on June 7, 1949, in the letter of Commissioner Davis to Congressman Walter, dated June 9, 1949, *H. R. Hearings on S. 1008*, at 60-62.

[180] The Journal of Commerce, in an editorial of June 8, 1949, was suspicious of the approval extended to S. 1008 by the Federal Trade Commission and of Senator O'Mahoney's sponsorship of the permanent legislation. See *H. R. Hearings on S. 1008*, at 68.

[181] *H. R. Hearings on S. 1008*, at 17 *ff*.

[182] *Ibid.*

of Tennessee tried to get Patman shut off[183] but without success.[184] Much of the questioning of Congressman Patman was heckling and argumentative. Congressman Robert J. Corbett of Pennsylvania, representing the Pittsburgh area, said that he supported the bill because "business does ask for an immediate decision on this problem,"[185] and a Congressman from Peoria, "where a number of large, bulky industries are operating," agreed with Corbett.[186] With these statements, which took an hour and a quarter, the Committee went into executive session and decided to report the bill favorably.

The bill was reported to the House, June 21, 1949.[187] The Committee report recommended the deletion of the Kefauver amendment[188] and spoke of clarification when it should have spoken of reversal of the courts. The *Cement* case, the *Rigid Steel Conduit* case, and the rule in the *Standard Oil Company* case were now all involved, since the bill would have given new defenses to those practicing freight absorption, making prices identical with those of competitors, and injuring competition, so long as "good faith" was present. The Kefauver amendment at least would have sustained the rule of the *Standard Oil* case. The O'Mahoney version would have reversed the rule of the *Standard Oil* case. As to *Rigid Steel*, Representative Walter said that the Federal Trade Commission was embarrassed to admit that it had made a mistake in pressing for favorable judgment on Count II in the *Rigid Steel* case.[189] The O'Mahoney Bill would probably have inhibited the Commission from proceeding against firms consciously paralleling prices, regardless of the effect on competition, where deliberate conspiracy was absent.

On June 30, 1949, the Rules Committee of the House granted an open rule providing for three hours general debate on S. 1008.[190] Representatives Celler and Walter of the Committee on the Judiciary urged the granting of the rule, and Patman opposed it unsuccessfully. The best he could do was make a speech warning the members of the House that S. 1008 was on its way.[191] He was active in another direction, however. As chairman of the House Select Committee on Small Business, he undertook himself to hold the hearings on S. 1008 which he said had been denied to him and to small business groups.[192] And for five days, witnesses made appearances before the Small Business Committee or sent statements attacking S. 1008. Professional economists,[193] representatives of small business organiza-

[183] *Id.* at 23.
[184] *Id.* at 24.
[185] *Id.* at 31.
[186] *Id.* at 35.
[187] 95 Cong. Rec. 8243 (June 21, 1949).
[188] H. R. REP. No. 869, to accompany S. 1008, 81st Cong., 1st Sess. 1 (1949).
[189] *H. R. Hearings on S. 1008*, at 27.
[190] 95 Cong. Rec. D640 (June 30, 1949).
[191] 95 Cong. Rec. 8936 *ff.* (June 30, 1949).
[192] Celler of New York found this maneuver "unseemly" because the Patman Committee was not a legislative committee, had no direct power to recommend legislation, and had no jurisdiction over S. 1008. Jurisdiction was in the Committee on the Judiciary, of which Celler was chairman. 95 Cong. Rec. 9164 (July 6, 1949).
[193] *Small Business Committee Hearings on S. 1008*, at 135, 212, 215.

tions,[194] wholesale and retail distributors,[195] the National Farmers Union,[196] the American Trucking Association, Inc.,[197] and staff of the Federal Trade Commission[198] made a record of protest of 300 pages, the theme of which was that S. 1008 would weaken the antitrust laws, cancel recent gains in the clarification of the laws, create more confusion and litigation, make it easier for violators to justify infractions, and harder for the Federal Trade Commission to halt such infractions. Walter Wooden, Associate General Counsel of the Commission, thought that S. 1008 would set back the Commission twenty-four years to the time of the *Old Cement* case.[199]

Having failed to prevent the granting of a rule to S. 1008, Patman then sought to delay the schedule of the Rules Committee in setting the time for the debate on S. 1008, but failed in this also.[200] In the course of discussing the schedule, however, Patman was able to forewarn the House of the principal objections that his select committee had developed.[201] He also kept the Appendix of the *Congressional Record* filled with editorials and extended remarks showing the impact of basing point systems on various geographical areas in the country.[202] The rule was called up as scheduled, and the House debate on S. 1008 began on July 6, 1949.[203]

The ignorance and confusion of the Congressmen in discussing the measure were depressing.[204] Brown of Ohio asserted that there had been "rather extensive hearings" on the bill before the Subcommittee and then the full Committee on the Judiciary,[205] which was not so. Sutton of Tennessee said that he had talked with the person in charge of the Antitrust Division of the Department of Justice by telephone the day before and had been told that the legislation was not necessary at all.[206] The attitude of the Department of Justice was variously expressed, and Walter of Pennsylvania asserted that Bergson had said that "it was absolutely necessary" that the bill be enacted.[207] This dispute was settled only when Majority

[194] *Id.* at 225.
[195] *Id.* at 3, 4, 9, 21.
[196] *Id.* at 75.
[197] *Id.* at 102.
[198] *Id.* at 30, 141, 202.
[199] *Id.* at 36. Cement Mfg'rs Protective Ass'n v. United States, 268 U. S. 588 (1925).
[200] 95 Cong. Rec. 9029 (July 5, 1949). Majority Leader McCormack hinted that Patman's request was tardy and that the bill might have been scheduled to Patman's satisfaction, had he been more prompt in his request.
[201] *Id.* at 9032 *ff.*
[202] *Id.* at A4451, A4452, A4477. See also 95 Cong. Rec. A3518, A3542, A3558 (May 31, 1949). Congressman Walter inserted a speech he made before the Pennsylvania Bar Association in which the decisions of the Federal Trade Commission on pricing were found to resemble the philosophy of a former Soviet Commissar of Justice. Special reference was made to Count II in the *Rigid Steel* case. S. 1008 was designed to combat the "Krylenko philosophy" represented by the Federal Trade Commission. 95 Cong. Rec. A4454 (July 5, 1949).
[203] 95 Cong. Rec. 9157-9172 (July 6, 1949).
[204] Congressman Lyle of Texas made an accurate observation when he remarked that "Generally, legislation coming to the floor under a rule is better understood than this particular bill." *Id.* at 9157.
[205] *Ibid.*
[206] *Id.* at 9158.
[207] The record of the hearings before the House Committee on the Judiciary does not disclose such a statement by Bergson. It does quote him as saying, "Insofar as the Department of Justice is concerned,

Leader McCormack declared that the bill had the approval of the Commission, the Department of Justice, the Bureau of the Budget, and the White House.[208] Patman said that O'Mahoney had "agreed to this substitute" (for the Myers moratorium) "only when the Kefauver amendment was added to it."[209] The record of course shows that he personally appeared before the House Judiciary Committee to get the Kefauver amendment stricken.

The chief accomplishment of the House was to write in another version of the Kefauver amendment after Patman failed to prevent the debate on the bill scheduled by the Rules Committee.[210] Willis of Louisiana led the first attack to restore the Kefauver amendment or another version of the amendment,[211] but this was defeated.[212] The second (and successful) effort to undo the work of the Committee on the Judiciary in striking out the Kefauver amendment was led by Carroll of Colorado.[213] The object of the Carroll amendment, as of the Kefauver and Willis amendments, was to deprive respondents under the Robinson-Patman Act of the defense of good faith where differential prices to meet those of a competitor (without differentials of cost) substantially lessened competition. Like the Kefauver and Willis amendments, its effect was to retain the rule of the *Standard Oil* case as decided by the Seventh Circuit Court of Appeals.[214] The Carroll amendment was adopted by the Committee of the Whole House[215] after a wearying debate in which few were on the floor and the speakers complained about the noise.[216] Since the House passed S. 1008 in a different form from the Senate, the measure was almost certainly headed for a conference committee unless the Senate accepted the House version.[217] This would have been true also if the Judiciary Committee

we have never urged the necessity or desirability of legislation with respect to the pricing practices to which the present bill is directed." *H. R. Hearings on S. 1008*, at 11.

[208] 95 Cong. Rec. 9164 (July 6, 1949). Patman was of the opinion that the Department of Justice was willing to restrict the operations of the Federal Trade Commission out of a sense of rivalry. *Id.* at 9227. He could not understand why the Federal Trade Commission had changed its position. *Ibid.*

[209] *Id.* at 9158.

[210] The vote on the rule was easily carried, *id.* at 9167, and the House proceeded to consider the measure on its merits, with time divided equally between opponents and proponents for three hours. *Id.* at 9168.

[211] 95 Cong. Rec. 9239-9240 (July 7, 1949).

[212] *Id.* at 9250. It is of interest that 143 Congressmen out of the total membership of 435 voted down the Willis amendment by a vote (on division) of 80-63.

[213] *Ibid.*

[214] 95 Cong. Rec. 9170 (July 6, 1949).

[215] 95 Cong. Rec. 9259 (July 7, 1949). The vote was 117-81. Where the Kefauver amendment had used the words "except where the effect of such absorption of freight will be to substantially lessen competition," the Carroll amendment said "except where such absorption of freight would be such that its effect upon competition may be that prohibited by this section." Where the Kefauver amendment used the words "other than a discrimination which will substantially lessen competition," the Carroll amendment said, "if the discrimination is not such that its effect upon competition may be that prohibited by this section." Compare Carroll amendments with S. 1008 as it passed the Senate, *supra* note 168. As S. 1008 passed the House, the phrase "substantial and probative evidence" in the definition of "the effect may be" had been changed to "reasonable possibility," thus restoring the rule of the *Morton Salt* case. See note 168 *supra*.

[216] See remarks of Christopher of Missouri, 95 Cong. Rec. 9256 (July 7, 1949), and White of Idaho, *id.* at 9258.

[217] The House passed the bill by voice vote after a motion to recommit to the Committee on the Judiciary was defeated. *Id.* at 9269.

version of the measure had been adopted intact by the House, since that version had eliminated the Kefauver amendment.

With the action of the House on the Carroll amendment, a sharp and fairly definite issue was for the first time joined. There was now a line, on one side of which the spokesmen for the Robinson-Patman Act could stand, and on the other, the spokesmen for legislative intervention on behalf of the steel, oil, cement, and building materials industries, all affected by recent decisions. The question was not now the abstract one of basing point systems and required f.o.b. pricing, nor freight absorption as such, nor moratoriums. After the action of the House, Senator Long of Louisiana warned the Senate that he recognized the existence of a drive to end the Robinson-Patman Act, and referred to a statement in the *Journal of Commerce* which spoke of Celler of New York as the sponsor of such a drive.[218] A statement attributed to Celler suggested that the conference committee might not have to take either the Kefauver or the Carroll amendments.[219] Long put the Senate on notice that he regarded the issue as a serious one and was prepared to make a fight on it.

On July 26, the Vice-President laid before the Senate the amendments made by the House to S. 1008, and McCarran of Nevada moved that the Senate disagree with the House and go to conference.[220] This was quickly agreed to by the Senate, and McCarran, O'Conor, and Wiley were appointed Senate conferees. Long and Kefauver immediately protested the action, charging McCarran with violation of an understanding to give notice to Kefauver when the conference vote would arise, to permit them instead to move to concur in the House amendments.[221] The McCarran motion to send the bill to conference, *sotto voce*, almost succeeded in preventing the Senate from debating S. 1008 at all. Senate protocol, had McCarran consented, would have nullified the vote to send the bill to conference. He, however, would agree only to a debate on Long's motion to reconsider, which is not a debate on the merits.[222] The debate was held on August 10, 11, and 12, and it failed to persuade the Senate to recall its decision to send S. 1008 to conference.[223] Before the matter was sent on its way to the House again with a request to appoint conferees, Senator Lucas of Illinois said that had he known the bill was going to cause so much trouble and take up so much time, it never would have got off the calendar. He had been persuaded to take it off the calendar by Senator Myers of Pennsylvania who had assured him "that it was a moratorium bill, which would probably require a couple of hours."[224] The weapon that McCarran had against

[218] 95 Cong. Rec. 9310 (July 8, 1949).

[219] *Ibid.*

[220] 95 Cong. Rec. 10387 (July 26, 1949).

[221] *Id.* at 10387-10388.

[222] See discussion of this point by Senator Morse, 95 Cong. Rec. 11496-11497 (Aug. 11, 1949).

[223] The motion to reconsider was rejected August 12, 1949. 95 Cong. Rec. 11553-11589 (Aug. 12, 1949).

[224] 95 Cong. Rec. 11376 (Aug. 10, 1949). Senator Lucas on two occasions tried and failed to get the debate limited by unanimous consent. He succeeded on the third attempt, but only after the supporters of the motion to reconsider had developed their attack at length. *Id.* at 11400, 11471, 11510.

the Long-Kefauver group throughout the three-day debate was the rule of the Senate that a motion to table the motion to reconsider would have the effect immediately of shutting off debate.[225] This advantage was not pressed, however.

The familiar ground was traversed once again, the chief difference being the new alertness of senators who had had the time and the inclination to inform themselves about matters upon which they had voted unknowingly when the O'Mahoney substitution for the Myers moratorium was made. O'Mahoney expressed again his interest in the development of trona deposits in Wyoming and his desire to make sure that Wyoming concerns would be permitted to absorb freight and quote delivered prices.[226] He also said that he thought his sponsorship of S. 1008 was consistent with his views when he was head of the TNEC. He said that he had been glad to accept the Kefauver amendment when it was introduced originally and hoped that it, or language like it, would come out of the conference committee intact.[227] He did not say that he had gone to the House Judiciary Committee to urge its removal.[228] Senator Myers said that he had no objection to either the Kefauver or the Carroll amendments but thought that the bill should go to conference because there were such deep cleavages on both sides.[229]

The principal speeches in favor of the motion to reconsider the vote to send the bill to conference were made by Senators Douglas, Long, Kefauver, Hill, and Morse. Senator Douglas, especially, made the most coherent and logical exposition to be made on either side of the controversy.[230] He took the bold view that the bill even with the Carroll amendment would legalize basing point systems, and that although the Carroll amendments improved the measure originally introduced, we would still be better off with no bill at all.[231] The principal instrument for the suppression of price competition is the basing point system, and this the

[225] *Id.* at 11377.

[226] *Id.* at 11394.

[227] *Id.* at 11395-11396.

[228] At still another place in the debate, on August 11, Senator O'Mahoney again said that he had accepted the Kefauver amendments in the Senate because he "believed they were totally in harmony with the purposes of the author of the substitute." 95 Cong. Rec. 11489 (Aug. 11, 1949). He failed to state at this time also that he had gone to the House Judiciary Committee to have the amendments stricken.

[229] 95 Cong. Rec. 11398 (Aug. 10, 1949).

[230] Senator Capehart was the originator of several short, sharp exchanges with Senator Douglas. The first exchange ended with the following colloquy: Mr. Capehart: "If the Senator wants an argument and a fight I will be very happy to give it to him. The Senator seems to be inviting it." Mr. Douglas: "I fight only in a good cause. If the Senator wants to take me on while I am defending a good cause, I am willing." 95 Cong. Rec. 11401 (Aug. 10, 1949).

[231] *Id.* at 11400. He mentioned trade-marked consumer goods like chocolate bars and other candies, chewing gums, cigars, soap, cosmetics, drugs, shirts, soft drinks and the like which sell all over the country at the same price (indicating freight absorption) and are protected by trade-mark. As to these the Federal Trade Commission had not proceeded against the uniform prices of trade-marked products and there was no prospect that it would. These are different from the standardized commodities in which there is little difference of quality, and price competition is the only kind that counts. Among the latter are steel, cement, lead, steel pipe and conduits, corn syrup, beet sugar, some forms of lumber, and brass. He said that the makers of the latter had been fighting behind the skirts of the first to legitimatize their own monopolistic practices.

O'Mahoney Bill, even with the House amendment, would sanctify.[232] The alleged confusion following the *Rigid Steel* case existed only in the minds of those sponsoring the O'Mahoney measure and not in the minds of the courts or the Federal Trade Commission. The fact that the Court split four to four in the *Rigid Steel* case need not have made legislation any more necessary than the four to four split in the Oregon minimum wage case in 1917.[233] Any further amplifications or refinements of statements about the law and its application should be undertaken by the administrative and the judicial processes. The present laws are adequate to deal with the situation and new legislation is unnecessary.[234]

Kefauver of Tennessee repeated many of the points that had been mentioned and developed some further.[235] The O'Mahoney Bill he thought was unnecessary. It added to and did not lessen confusion. But if it should be enacted, it should contain the Carroll amendments. The junior Senator from Tennessee in fact thought that the Carroll amendments were broader and provided more protection to small business[236] than his own. Kefauver reviewed the cases which the O'Mahoney Bill would affect (indeed, set aside) including the familiar five: *Corn Product*, *Staley*, *Cement*, *Rigid Steel*, and *Standard Oil*—in short all of the cases in which the profile of the law was becoming more and not less clear and certain.[237] Like Douglas, Kefauver hoped that the bill would be defeated. The minimum condition of acceptance, he felt, should be the adoption of the Carroll amendments.[238] There was a strong implication that the Senators sponsoring the bill did not know what they were doing when Kefauver said that the purpose of the measure was to emasculate the antitrust laws, a purpose that the sponsoring Senators did not embrace, but which was the design of "the great lobby that is behind the bill."[239]

[232] Douglas cited a letter written to him at his request by the Chairman of the Department of Mathematics at Haverford in which it was estimated that the probability of eight identical bids in 102 counties was one in eight followed by 214 zeros. The Illinois Department of Highways in 1947 had received bids from eight cement companies which were identical within each of the 102 counties in the state. *Id.* at 11403.

[233] Stettler v. O'Hara, 243 U. S. 629 (1917).

[234] 95 Cong. Rec. 11405 (Aug. 10, 1949). The Kefauver and Carroll amendments would only have "limited the bare-faced use of the basing point system," not made it obviously unlawful. *Id.* at 11408. Capehart said that Douglas was confusing the right of individual sellers acting independently to absorb freight with the basing point system. There is perhaps less confusion than overlapping between the two. Not all freight absorption is basing point in structure, but typical basing point systems involve freight absorption. A bill making all non-conspiratorial freight absorption lawful regardless of effect on competition could be understood to legalize basing point systems, as Douglas asserted. 95 Cong. Rec. 11412 (Aug. 11, 1949).

[235] Kefauver's principal presentation is to be found in 95 Cong. Rec. 11475 *ff.* (Aug. 11, 1949).

[236] *Id.* at 11477. When he first proposed his amendment Kefauver proposed to insert the words "except where the effect of such absorption of freight will be to substantially lessen competition." He then thought that the word "will" was incorrect since the word "may" customarily appears in antitrust legislation, and substituted the word "may" for the word "will" in the printed copy of his bill. It was adopted by the Senate with the word "will," however, raising a matter of some concern to the conference committee when it looked for a version of the Kefauver-Carroll amendments that would be satisfactory to both the House and the Senate.

[237] *Id.* at 11476.

[238] *Id.* at 11485.

[239] *Ibid.*

Hill of Alabama and Morse of Oregon made the last two speeches of importance in favor of the motion to reconsider. Hill drew freely upon the views of witnesses before the Patman Small Business Committee,[240] and the reported views of the Federal Trade Commission,[241] the Department of Justice,[242] and the press.[243] Morse of Oregon, although feeling that the bill would eventually pass into law,[244] nevertheless conducted a vigorous attack upon it. He deplored what seemed to him to be a breach of the usual senatorial practice when sentiment exists to reconsider a vote by which bills are sent to conference. The customary practice he had found was to permit reconsideration by unanimous consent, without debating the motion.[245] This courtesy had been withheld by the chairman of the Senate Judiciary Committee, who had originally called for a vote on sending the bill to conference when Kefauver, with whom he had had an agreement to give prior notice, was not in his seat.[246] Morse wanted the record to show that the proponents of the bill wanted to take refuge in the protection of a technicality in the rule.[247]

Morse preferred the Carroll amendment to the Kefauver amendment because the latter contained the inadvertent word "will" and he applauded Kefauver's forthrightness in accepting the Carroll amendment in place of his own.[248] He made an exposition of the actual operation of basing point systems,[249] thereby carrying forward the excellent lecture given to the Senate by Douglas and others on economics. He twitted O'Mahoney with a news release issued by the Senator from Wyoming and dated July 11, 1948, in which the basing point system was condemned, the reader was warned that the steel industry would try to lay the basis for a demand that Congress change the antitrust law, and the case was made for a good faith abandonment of the basing point system in favor of f.o.b. pricing.[250] He thought that the news release left some in doubt as to how the Senator from Wyoming could justify his position on S. 1008.

On the last day of the three-day debate on the motion to reconsider, the time was divided equally (under a unanimous consent agreement) beween the supporters and opponents of the motion. Wherry of Nebraska led off against the motion to reconsider by asserting that the bill (S. 1008) had been used as a medium for

[240] *Id.* at 11490, 11495.

[241] *Id.* at 11491.

[242] *Ibid.*

[243] *Id.* at 11495.

[244] In a colloquy with Senator Douglas, Senator Morse said: "But I am sure the Senator from Illinois will agree with me that the probabilities are that Senate Bill 1008 will be finally passed by the Senate." *Id.* at 11498. And again, "But I recognize that a bill is going to be passed, and therefore I am going to do the very best I can to patch it up." *Id.* at 11503.

[245] *Id.* at 11496.

[246] *Id.* at 11497.

[247] Long of Louisiana was also absent, being "on my way to the Senate Chamber at the time the motion was made." 95 Cong. Rec. 10387 (July 26, 1949). The agreement was made between McCarran and Kefauver. Russell of Georgia had also asked McCarran to be notified. Long spoke of the "low tone of voice" in which McCarran had put the motion to send the bill to conference. *Id.* at 10388.

[248] 95 Cong. Rec. 11498 (Aug. 11, 1949).

[249] *Id.* at 11498-11508.

[250] *Id.* at 11508-11509.

airing wholesale violations of the antitrust laws. He thought that S. 1008 was designed to restore the competitive conditions "which were revolutionized by the Supreme Court opinion in the *Cement* case."[251] The issue was a simple one, and he proceeded to explain it in terms of horse trading on the farm. Douglas made a summary of his previous speech.[252] O'Conor of Maryland concentrated upon the Carroll amendments which he thought meant to "amend the Robinson-Patman Act except in any respect in which it is in force."[253] Among the authorities invoked in favor of S. 1008 was John D. Clark of the Council of Economic Advisers, described by Johnson of Colorado as a great liberal who, although his father left him a fortune, "did not become a playboy at all."[254]

The suggestion made the day before by Morse, that Senator O'Mahoney was professing a view inconsistent with that he held on July 11, 1948, was further developed by Long.[255] O'Mahoney maintained his position that S. 1008 contained nothing which affected the basing point system or the multiple basing point system.[256] He argued that if S. 1008 were defeated, steel could go back to f.o.b. mill prices and then prevent any other state from developing a steel industry.[257] It was put to him that he had once said that it was best for the steel companies to go on an f.o.b. pricing basis. O'Mahoney's answer was that the TNEC report had indicated that a change in f.o.b. pricing must allow industry time for adjustment. He saw around him now opportunities for new competitive enterprises to enter industry, and believed that they could not do it without being permitted to absorb freight.[258]

Sparkman of Alabama reviewed the history of the pressure which had been organized to produce changes in the antitrust laws by Congress.[259] He paid special attention to the effect of the abolition of the basing point system on the sugar beet industry of Colorado, Wyoming, and other Mountain States and concluded that the result would not be harmful to that industry in those states.[260] This seems to have been an appeal to the chief proponents of the legislation from important sugar beet states, Johnson of Colorado and O'Mahoney of Wyoming. Pepper of Florida developed the case against the basing point system with special reference to Florida.[261] With some further remarks by Long and Kefauver, the struggle to

[251] 95 Cong. Rec. 11554 (Aug. 12, 1949).

[252] *Id.* at 11557-11559.

[253] *Id.* at 11563.

[254] *Id.* at 11492. See testimony of Clark cited by O'Conor, *id.* at 11563. Long of Louisiana suggested that Clark was one of the "great Standard Oil executives," who had been "one of the foremost advocates of the legalization of the basing-point system itself" and that if the bill met with Mr. Clark's approval that fact might "indicate that the bill might actually legalize the basing-point system." *Id.* at 11492.

[255] *Id.* at 11572.

[256] *Id.* at 11573.

[257] *Ibid.*

[258] *Ibid.*

[259] He also utilized the material reported by James W. Daniel, Washington correspondent of the Rocky Mountain News, Dec. 17 and 22, 1948, describing the activities of an organization which set out to produce a "grass roots demand" for change in the law. *Id.* at 11575.

[260] *Id.* at 11575-11578.

[261] *Id.* at 11579-11582.

get the Senate to reconsider the motion to send the bill to conference ended. It was a struggle that had been waged in the main by Senators from southern and midwestern states against Senators from the steel and beet sugar states.

Before the vote was taken on the motion to reconsider, McCarran undertook to defend O'Mahoney, as Johnson had previously done.[262] The McCarran statement was notable chiefly for the suggestion that the O'Mahoney Bill was more anti-monopolistic than "any bill which was likely to come out of the Committee on the Judiciary after the year of study which was contemplated during the period of moratorium" which the Myers Bill would have provided.[263] The motion to reconsider the vote to send S. 1008 to conference was lost 28-49,[264] and McCarran was stopped by Langer of North Dakota in a maneuver to have O'Mahoney and Jenner of Indiana added to the conference committee.[265]

VII

THE CONFERENCE REPORT

The final passage at arms in the First Session of the Eighty-first Congress took place over the conference committee report which was submitted in the closing days of the session.[266] As reported by the conference committee, the compromise bill was unacceptable to Celler, chairman of the House Judiciary Committee, and Willis of Louisiana.[267] It was acceptable to the three Republican conferees and one Democrat, Representative Walter of Pennsylvania, who was on the high seas but had cabled his proxy, not to a member of his party, but to a member of the minority party.[268]

S. 1008, as finally proposed in the conference report, amended the Federal Trade Commission Act to provide that it should not be regarded as an unfair trade practice for sellers acting independently to absorb freight and quote delivered prices.[269] Language withheld the benefits of the Act from any combination, conspiracy, or collusive agreement, and from any monopolistic, oppressive, deceptive, or fraudulent practice carried out by the use of freight absorption or delivered prices. This

[262] Johnson had said, "The chemical industries of the West wanted to go ahead without further delay. They had to have matters clarified so they could develop the industries they had in mind. Industries wanted to get under way in Wyoming. They were demanding that the matter be settled. They persuaded the Senator [*i.e.*, O'Mahoney] they needed action at once and the present bill is the result. *Id.* at 11573.

[263] *Id.* at 11583.

[264] *Id.* at 11588.

[265] McCarran asked for unanimous consent to augment the number of Senate conferees and to add Jenner and O'Mahoney, but Langer objected and unanimous consent was therefore not secured. *Id.* at 11589.

[266] After the Senate action sending the measure to conference, the House insisted on its amendments, agreed to the conference (95 Cong. Rec. 11811 (Aug. 16, 1949)) and appointed conferees, August 16, 1949. The conference report, H. Rep. No. 1422, was submitted to the House on October 14, 1949, and debated. 95 Cong. Rec. 14786 (Oct. 14, 1949).

[267] 95 Cong. Rec. 14786 (Oct. 14, 1949).

[268] Michener of Michigan. Walter's views about the legislation were closer to those of Michener than to either of the other two conferees of his own party. See Michener's statement, *id.* at 14794.

[269] *Id.* at 14794-14795.

language had been included in both House and Senate versions of S. 1008. The Robinson-Patman Act was amended to make it lawful for sellers independently to absorb freight or quote delivered prices unless the effect of these practices "upon competition will be to substantially lessen competition." This was the version of the Kefauver amendment that Kefauver had repudiated. Even where the forbidden effect was shown, however, the conference report provided that good faith meeting of the lower prices of a competitor should be a complete defense to a charge of unlawful discrimination, regardless of its effect upon competition. It was therefore possible for the Federal Trade Commission to prove a prohibited discrimination to which good faith would be a complete defense.

The press reported (as the conference report indicated) that S. 1008 would overrule the Seventh Circuit Court decision in the *Standard Oil* case, where a prohibited effect upon competition vitiated the defense of good faith in a charge of unlawful price discrimination.[270] Moreover, language of the proposed bill required the Commission to demonstrate illegal effects of price discrimination with "reliable, probative and substantial evidence." This threw out the rule of the *Morton Salt* case, where the Commission had been required to prove only a "reasonable possibility" that the effect of a price discrimination would injure competition unlawfully. The general exemption extended to non-conspiratorial freight absorption would have nullified the holding on Count II in the *Rigid Steel Conduit* case, and would have weakened the theoretical basis of the *Cement* case, and the *Glucose* cases which preceded it.

Carroll of Colorado supported Celler's objection to the conference report and explained the circumstances under which the word "will" had come into the Kefauver amendment instead of "may." He proposed that the report be recommitted or that no legislation on the subject at all should be sought.[271] Others felt as Carroll did.[272] Strong statements in support of the conference report were made by Halleck of Indiana[273] and Michener of Michigan.[274] The proceedings were short, and after a motion to recommit was lost,[275] the conference report was adopted by the House by a vote of 200-104.[276]

With the submission of the conference report to the Senate,[277] the opponents of S. 1008 had picked up another ally—time.[278] The Senate was in the last days of the First Session of the Eighty-first Congress, and the Congressmen wanted to expedite their business in order to get home. O'Conor was reported to be confident

[270] Wall Street Journal, Oct. 13, 1949, p. 8, col. 2.

[271] 95 Cong. Rec. 14788 (Oct. 14, 1949).

[272] For example, Boggs of Louisiana, *id.* at 14789.

[273] *Id.* at 14789-14790.

[274] *Id.* at 14794-14796.

[275] *Id.* at 14797. The vote was 138-178, with 116 not voting.

[276] *Id.* at 14797-14798. There were 128 not voting.

[277] 95 Cong. Rec. 14983 (Oct. 15, 1949).

[278] See 95 Cong. Rec. 15054-15055 (Oct. 17, 1949), where Lucas of Illinois arranged the schedule of the Senate, including the conference report debate.

that he had enough votes to push the bill through.[279] The pressure was so great that the sponsors of the conference report actually managed to slip it through the Senate in a Saturday night session with what Douglas described as "supersonic speed."[280] The action was recalled by the timely attentiveness of Douglas and Long. The Senator from Illinois said that he and Long were standing close to the Chair, but even then could not hear the question which was stated, "and we were startled by the almost instantaneous announcement that the report had been agreed to." This tactic was reminiscent of the manner in which the motion to send the bill to conference had been maneuvered. If Douglas and Long had not been watching for the Saturday night motion, the Senate would have enacted a fundamental reform of the antitrust laws that had never had hearings in either the House or the Senate, which few legislators understood, and which had been put on the books by inadvertence.

The last debate on S. 1008 began when Douglas objected to the conference report in its entirety.[281] He expressed the opinion that S. 1008 legalized the basing point system, the postage stamp and zone systems of pricing, and would produce a reversal of the entire policy of the government in the pricing field.[282] In addition, he felt that the bill really repealed the Robinson-Patman Act.[283] Hill of Alabama contributed a recollection of William Jennings Bryan who once in a debate against a tariff bill referred to the banyan tree which entices the unwary native to seek its fruit only to be crushed by the powerful limbs of the tree.[284] Capehart wanted to talk about the Miller-Tydings Act which Douglas suggested was as relevant to S. 1008 as canasta.[285] As he had warned in an early phase of his speech, Douglas at its conclusion moved that further consideration of the conference report on S. 1008 be postponed until January 20, 1950.[286] O'Conor immediately moved to table the motion and on the yeas and nays, the motion was lost, 29-29, the Chair indicating that its vote would be in the negative.[287]

The denouement was supplied by O'Mahoney who turned against the bill he had sponsored, and gave his support to Douglas. He expressed his pleasure that the Douglas motion was not laid upon the table,[288] and he urged that it be adopted.

279 The Journal of Commerce, Oct. 18, 1949, p. 2, cols. 6-8. Senator Long told reporters that Douglas would not filibuster, but that he had no objection to doing so. See also Journal of Commerce, Oct. 19, 1949, p. 1, col. 8, where mention is made of a sizable stack of books brought to the Senate by Long.

280 95 Cong. Rec. 15115 (Oct. 17, 1949).

281 Douglas got unanimous consent to hold the floor on October 17 and to permit him to resume the debate the next morning, October 18. *Id.* at 15118.

282 *Id.* at 15165-15166.

283 *Id.* at 15167.

284 *Id.* at 15168. Douglas thought that this illustration was more graphic than the spider and fly analogy.

285 95 Cong. Rec. 15168 (Oct. 18, 1949).

286 Douglas' first motion was to recommit the report to the conference committee with the request that it report on January 20, 1950. This was ruled out of order since the House had already acted. *Id.* at 15173.

287 *Id.* at 15174.

288 *Ibid.*

His principal point was that the conference committee version of S. 1008 permitted the Federal Trade Commission to proceed against prohibited forms of freight absorption only where the effect of the absorption *will* be to lessen competition substantially, not where there might be a reasonable probability of this result.[289] The committee had retained the original or inadvertent version of the Kefauver amendment; O'Mahoney thought that the Carroll version was preferable. O'Mahoney warned that if consideration were not postponed, he would have to vote against the bill that he had introduced.[290] The conference bill not only did not clear away misunderstandings, but created fresh ones. O'Mahoney said that he had always understood independent freight absorption to be legal and was glad to have the recent opinion of the Fourth Circuit Court of Appeals in the case of *Bond Crown and Cork Company v. Federal Trade Commission* confirm this belief.[291] He concluded by explaining why he had got into the controversy in the first place—Wyoming beets and chemicals[292]—but now felt that the conference report version of his bill would work to the disadvantage of these industries by "locking up the natural resources of the West in the hands of the monopolists." This statement (perhaps it might be called "recantation") was documented by a letter from O'Mahoney to Mr. Robert D. Pike, in which the latter was assured that the courts, the Commission, and the Department of Justice would continue to support the legality of independent freight absorption.[293]

With the conclusion of O'Mahoney's speech, the opposition to Douglas' motion collapsed. The Senate quickly agreed by voice vote to postpone consideration of the conference report to January 20, 1950.[294]

VIII

SUMMARY AND CONCLUSION

The drive to amend the antitrust laws and overrule major decisions of the Federal courts was begun in the summer of 1948 when steel customers, and others, stimulated by the new pricing policy of the steel industry, appeared on the stage of the Capehart Committee and asked that Congress "clarify" the law on pricing. The trouble was not really that the law was unclear but that it was becoming more clear as the Federal Trade Commission and the courts applied the Federal Trade Commission and Clayton Acts (as amended) to new situations. The principal effect of the two measures to enact permanent amendment of these statutes—S. 236 and O'Mahoney's S. 1008—would have been to set aside the new decisions. A trend was to be stopped and perhaps reversed, not made more viable in the directions freshly opened.

289 *Id.* at 15174-15176.
290 *Id.* at 15176.
291 176 F. 2d 974 (C. C. A. 4th 1949). 95 Cong. Rec. 15176 (Oct. 18, 1949).
292 95 Cong. Rec. 15176 (Oct. 18, 1949).
293 *Id.* at 15179-15180.
294 *Id.* at 15180.

After the somewhat elaborate propaganda prepared by the Capehart hearings for a Congress that the voters did not elect, the effort to write a permanent statutory amendment of the antitrust laws proceeded briefly, but was soon abandoned because of the complexity of the problem and the desire of the proponents of change for quick results. The Myers moratorium was to serve this desire. At the critical point, however, the proponents of legislative intervention against the Commission and the courts found themselves being led, to their joyful surprise, by Senator O'Mahoney, who seems to have been influential in bringing along the Commission and the Department of Justice also. If Kefauver had not amended S. 1008, however inadvertently, as it whisked through the Senate, one of the fastest breaking squeeze plays in recent legislative history would have reversed developments in the law of pricing that had taken years to mature. The Kefauver amendment slowed up proceedings in the House, made a conference necessary, and thereby gave time for an opposition to crystallize and organize. Even with this small gain, two strategems threatened to prevent the new opposition from placing its weight against the insistent thrust to legislate. These were the maneuvers that almost sent S. 1008 to conference on tiptoe, and then almost whirled the conference report through the Senate with "supersonic speed."

Few Congressmen seemed to know quite what they were doing, and on S. 1008, at least, there was almost no way for them to find out, since the O'Mahoney Bill was given no hearings in the Senate and no public hearings in the House Judiciary Committee. The only public hearings it received were held by a committee that had no jurisdiction over the measure. The Capehart hearings were useless as a basis for legislation. The residuum which the Capehart hearings leave is that the witnesses, understandably, would feel uncomfortable in the dream world of required f.o.b. pricing that was imagined for them. The hearings on S. 236 were perfunctory at best, and full investigation of alternatives was missing.

The Federal Trade Commission looked no more sure of itself at points than some of the Congressmen. Under pressure, the Commission seems to have abandoned at least one position that it assumed before the courts, and permitted itself to be reported as not in objection to the O'Mahoney Bill, although it had declined to support either S. 236 or the Myers moratorium. Moreover, direct statements were made in Congress to the effect that the Commission staff was responsible for language in the O'Mahoney Bill. Without a full knowledge of all of the considerations that seemed to be pressing and important, it is impossible to judge the necessity of the Commission's choice. The student of antitrust policies may be permitted the hope, however, that the Commission will not lose sight of the trust given it by the statutes to carry forward, not backward, the enforcement of the laws governing competition.

It need not be supposed that those who supported the O'Mahoney Bill were willful wreckers of the antitrust laws, for the choices were not simple and clear-cut. Few argued that required f.o.b. pricing was desirable. Most accepted the view that

independent freight absorption made in good faith with no adverse effect upon competition was desirable. But neither Johnson, Myers, nor O'Mahoney succeeded in producing a bill to protect this kind of freight absorption without at the same time lending countenance to practices that would be restrictive of competition, be hard to detect, and be harder to prove. It is not difficult to understand that the harassed Congressman, importuned by restless constituents, would prefer to risk abuse of the law if he could protect the concerns of the innocent in intention. Indeed, O'Mahoney himself seems to have made somewhat this kind of choice. The alternatives, however, become a little clearer when it is established that the fears are unfounded. One does not then have to assume the risk. This is the view with which O'Mahoney started. It is the one with which he finished.

A reasonable case can be made for the proposition that the entire antitrust policy of the United States should be reviewed candidly, re-formulated in the light of sixty years' experience, and fitted to suit the requirements both of large scale industry and the public in the middle of the twentieth century. It may be that the complications swamp the benefits of legislation in the pricing field that is too detailed and specific. Free enterprise is a valuable concept which certainly should not be impaired by the very laws enacted to fulfill its promise. But the formulation of new policy requires at the least comprehension of the issues, full hearing for all relevant views, and an earnest effort in good faith to reach a new balance of interests. The movement to change the law on pricing in the First Session of the Eighty-first Congress fulfilled none of these conditions.

BOOK REVIEW

THE BASING-POINT SYSTEM. By Fritz Machlup. Philadelphia: The Blakiston Co., 1949. Pp. 275. $5.00.

In this valuable book Professor Machlup gives us a comprehensive analysis—and a forceful condemnation—of the basing-point system of pricing in the United States, a system whose merits are today being disputed in Congress. This is no fly-by-night book; the material included is part of a large volume of material which Machlup has been gathering over a period of years for a forthcoming book on the general subject of price discrimination. The author with the cooperation of The Blakiston Company rushed the basing-point sections of the analysis into print so that the economist would have his day in court before and not after the legislative decision was reached.

At times one is sadly forced to conclude that jurists, legislators, lawyers, businessmen, editorial writers especially, and even economists do not make sense because they have no sure grasp of even the most elementary mechanics of the basing-point system. Machlup's first task is to set down the terminology and operating rules of the system. To this reviewer's knowledge Chapter 1 is the best currently available systematic explanation of these fundamentals.

Although Machlup recognizes and briefly treats the interplay of legal, business, economic, and political factors in the present controversy, he has argued his case mainly on the grounds of theoretical economic considerations. His first major concern is with the "monopolistic"[1] nature of the animal. He reviews the old errors which have made it possible in honest confusion to identify the price uniformity resulting from the basing-point system as evidence of competition. And he lays the bogy of "local monopoly," which the basing-point system is alleged to prevent.[2] He notes the significant inconsistency of industry statements that (1) the basing-point system is competitive and (2) frequent deviations from the fixed basing-point price in the form of "price-shading" introduce competitive elements into a seemingly rigid system.

Machlup's second major concern is with the "discriminatory" nature of the basing-point system. His simple test of non-discrimination is the lack of interest of a seller in the functional, geographic, racial, and other characteristics of the buyer. The seller under the basing-point system, of course, cannot meet this test since he is quite interested in the buyer's place of business and quotes delivered prices which do not equalize his mill net but which conform to the established basing-point price. As seen in footnote two above, the basing-point method of pricing *systematically* operates to discriminate against a consumer located near a non-base mill. Another type of discrimination is against consuming areas in which the substitute products of another industry are unavailable or consuming areas in which the expansion of capacity is not welcomed by the large producers. Suppose that a small Chicago producer in a basing-point industry dominated by a large Pittsburgh firm were to attempt to build up its volume by announcing a new, lower basing-point price at Chicago. Under the basing-point system

[1] Monopoly for him is the extent to which there is a oneness in decision-making in an industry, whether because of the dominance of one firm or because of the practice of forming decisions in the light of how other firms in the industry are expected to react.

[2] Crudely speaking, under the basing-point system a consumer located near a non-base mill is able to select among many sellers located at varying distances, all of whom charge the high, monopolistically established price, while under a uniform f.o.b. system he would be quoted many different prices and would presumably choose the low price of the near-by "local monopoly" seller.

the Pittsburgh producer would meet the new low delivered price by absorbing freight[3] on shipments into the Chicago area, and would step up selling efforts or would resort to price-shading in order to punish the upstart. Even if the Pittsburgh firm took no punitive action, the working of the basing-point system would automatically lead to its accepting a lower mill net in sales to the Chicago area, a clear case of built-in local price discrimination concealed under the socially acceptable guise of "meeting competition in the Chicago market!" The average mill net of the Pittsburgh producer would be cut slightly, that of the Chicago firm greatly. Hence the Chicago firm will be induced to go along with the Pittsburgh basing-point price or a high Chicago basing-point price and to be content with its normal share of the industry's volume of business. And the Chicago customers of the industry will be discriminated against.

Secret price deals outside the basing-point framework are most often in recognition of the power of large buyers. This type of price discrimination is not a feature of the basing-point system per se.

Machlup's third major concern is with the waste of economic resources arising out of the basing-point system. The first of these wastes that usually comes to mind, "cross-hauling," involves many little byways of economic analysis that the author treats briefly. Other wastes considered are the uneconomic location of industry capacity and the uneconomic location of buyers' places of business.

A fourth major concern is the concentration of economic power under the basing-point system. Machlup demonstrates how small firms are encouraged to merge with large, how small firms are discouraged from expanding, how entry to the industry is made less attractive, and how "special" prices are likely to favor the larger buyers.

The author regards compulsory uniform f.o.b. pricing as the only desirable practical alternative to the basing-point system. He does not go into detail as to the methods and degrees of compulsion or uniformity.

One of the extremely interesting economic aspects of f.o.b. pricing is whether or not it would lead to "ruinous competition." First, it should be recognized that industrial monopoly and uniform f.o.b. pricing may exist together.[4] The prevention of further merger and perhaps some fractionalization of industry presumably would be prescribed also if one went along with uniform f.o.b. pricing. These problems Machlup recognizes. He believes that the danger of "ruinous competition" is overrated. Among other things he points out that under a uniform f.o.b. system a firm which must cut prices on all near-by safe business in order to extend its market boundaries will hesitate taking the action, the more so if it may reasonably expect retaliatory price cuts by rival sellers.[5]

It is not to be expected that Machlup would present as complete an analysis of the various facets of the uniform f.o.b. system as he does of the basing-point system. He does not, for instance, consider the vexing problem of what to do about large buyers of an industry's product if the industry is compelled to adopt a uniform f.o.b. price system. Would buyers be prevented from exerting monopsonistic pressure in the form

[3] Machlup explains why neither "freight absorption" nor "phantom freight" are unambiguous terms.

[4] It is apparent that the ease with which monopoly is established, the kinds of monopoly, and the effects of monopoly would differ considerably under the basing-point and monopoly type f.o.b. systems.

[5] Much different is the point of view of Professor John M. Clark, a leading scholar in the field of industrial price policy, who feels that any such sharp break with the basing-point system would probably bring destructive price wars, great dislocation of labor, and a radical readjustment of investment values. See, for example, his *Basing Point Method of Price Quoting*, 4 CAN. J. ECON. AND POL. SCI. 477 (1938). Professor Clark feels that the presence of large overhead costs and the economic strength of large buyers make a considerable measure of restriction inevitable in these industries.

of paying different delivered prices for their purchases of a product? What about the existence of monopolistic suppliers of raw materials and labor services who might hold the whip hand over a chastised, fractionalized, ex-basing-point industry?

A major issue Machlup mentions is the increase in government "interference" that a compulsory f.o.b. pricing system would entail.[6] On this point is not FDR's dictum applicable, namely, that "the minimum regulation businessmen can expect is the preservation of competition?" Machlup, as an "old-fashioned liberal," is probably going to be increasingly unhappy as few forces emerge to block the movement toward Bigger Business, Bigger Labor, and Bigger Government.

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[6] The author expresses his own credo (p. 50) as being ". . . old-fashioned liberalism: an unbounded respect for political and economic freedom, a belief that a truly competitive order is not only the best guarantee for the preservation of freedom but also the most efficient mechanism for the allocation of economic resources, a conviction that private property and free private enterprise are necessary for the working of a competitive order, a disrepect for vested interests . . . and a confidence that a free society can be established and maintained by a people who insist on a wide dispersion and decentralization of economic and political power."